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- **Gross Income Estimates in the Valuation of Stores**
- **The Valuation of Hospitals**
- **The Folklore of Valuation**
- **What Makes the Hot Spot "Hot"?**
- **The Supermarket**
- **Has Land a Value?**
- **Appraisal of Department Stores**

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The APPRAISAL JOURNAL

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This publication is provided as a medium for the expression of individual opinion concerning appraisal practice and procedure and topics allied thereto. The articles printed herein do not necessarily represent the endorsement of the Institute or of the majority of the members excepting as such statements may be designated as approved by the Governing Council. The editors exercise only a general supervision of the material and assume no responsibility for the opinions expressed by the contributors.

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ANNOUNCING A LECTURE COURSE ON THE MANAGEMENT OF UNFURNISHED APARTMENTS

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HOTEL PRESIDENT — KANSAS CITY, MISSOURI

December 4, 5, 6, 7, and 8, 1939

Examination for Membership in the Institute, December 9

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For detailed information address

THE INSTITUTE OF REAL ESTATE MANAGEMENT
22 West Monroe Street, Chicago, Illinois

· With the Editors ·

ON THE HOUSE

MANY of the large fire insurance companies are now adding the "come-on" of *free appraisals* to their usual ballyhoo for new and more business. Of course, it is the same old story of giving something for nothing in order to effect a sale. Our recorded history does not go back far enough to disclose the origin of the fundamental idea, but it is still good, and the public is falling for this variation — and falling hard.

It seems that the annual premium covers everything, including the cost of the appraisal required to determine the insurable value, and thereby the assured saves an appraiser's fee. The answer, of course, is that the premium is set to cover the added cost to the company—assuming that an actual and intelligent appraisal is made. It is more than probable that it also includes an added profit on this extra service. Obviously the cost must come in somewhere since the insurance companies are not generally recognized as charitable institutions.

No, the idea is not new. One of the most successful applications of this ancient thesis was the "free lunch" of that happier era before the saloon became a tavern. Some no doubt can recall with us the good old days when we pushed through the double swinging doors and faced a groaning board of real food and rare delicacies—a veritable Swedish smörgåsbord. It was free to everyone if he bought a beer, and that cost him only a nickel! Where was the "joker"? Well, that came in the evening—say after the theatre, when he came back with a party of convivial friends and left a five-spot as his contribution. Incidentally this time nobody was hungry! And every once in a while Jerry would mop up the bar and say: "Well, boys, this one is on the house." Remember? He was a good salesman, too, and knew the night's receipts would easily cover the extra cost plus the expected percentage on the whole.

The amazing part of this insurance thing is not that the purchaser is willing to accept blindly the company's figure as a sound and proper appraisal upon which to base his insurance—it is rather in the fact that the companies themselves would countenance the practice. Certainly this is no "arm's-length" transaction. By its very nature the appraisal must be viewed as partisan since it is made by one of the parties at interest. Furthermore, the insurance business is one vested to a large extent with public interest. It is subject to regulation, and its dealings should be such as to avoid any possibility of criticism.

This growing practice of "free" appraisals may not violate the letter of the laws regulating the insurance business, but it puts an awful strain upon the spirit of impartial public relations. And none knows better than the members of the insurance fraternity what the maintaining of that spirit means in terms of premium dollars. For the good of both the public and the insurance companies, we hope this is but an experiment in applied sales psychology that may soon be returned to a shelf in the laboratory.

THE APPRAISER'S RESPONSIBILITY

A REAL estate appraisal is an opinion of value. An opinion is a conviction founded upon probable evidence. It is stronger than an impression, not as strong as positive knowledge, and is not susceptible of definite proof.

The assumption of greater responsibility for justifying and defending opinions of value will be beneficial to the appraisal profession and induce greater public confidence, but there appears to be a growing tendency, particularly on the part of institutional lending officers, to practice the old army game of "buck passing" as a cover up for their own ineptitude.

The appraiser is the last man in line. He has no one to whom he can pass the buck. A conscientious appraiser reports his impartial opinion of value as of a certain date, for a certain purpose, after duly considering all the pertinent data. Future events can, of course, make wise men of fools and fools of wise men, but they do not in themselves prove that the appraiser was in error at the time his valuation was made.

Lending officers are heard to complain that appraisals are getting too high and loans too large. We ask: "How do they know this is true, and, if it is true, why do they make loans based upon such appraisals?"

They further complain that insufficient supporting data are furnished with the report. We ask: "Why do they accept such reports, and why do they not insist that the report state that it is made for mortgage-lending purposes?"

They complain also that the appraiser is being influenced by borrowers and mortgage brokers. If this is true, their own policy of naming the appraiser and forcing the borrower to pay the bill may well be a contributing factor.

Is it possible that these lending officers wish to shift the responsibility to the appraiser? If this is true, we need a new crop of lending officers.

If a mortgage goes "sour," the tendency is to get out the appraisal upon which the original loan was based, compare it with today's value, and say, "My God, no wonder we are stuck!" The reason for the failure may be overfinancing due to an overvaluation, but it may be due to a number of other causes which are in no way the responsibility of the appraiser.

Too low amortization to margin properly a depreciating asset, unwillingness to foreclose promptly, thus permitting the property to be milked, the demand for excessive interest rates at the expense of amortization, and in general permission of the loan policy to be dictated by competition instead of sound judgment are a few of the causes of loan failure which are not the fault of the appraiser.

The appraiser and the lending officer must supplement one another, and nothing is to be gained by either one passing the buck to the other.

●

THE VOICE OF EXPERIENCE

AS APPRAISERS we are attuned to economic changes and business adjustments. In our everyday practices we are constantly attempting to assemble factual data for analysis and interpretation in terms of future probabilities. In this endeavor we relate these data and form our conclusions principally upon the basis of the experience gained under comparable situations of the past. We know that the pendulum will swing both ways, the degree of the arc and the time consumed in the process depending upon the length of the arm and the motivating forces.

Europe is again at war. This certainly means major adjustments in the value structure. What does this in turn signify to the appraiser? Undoubtedly it means that the basic standards which have guided our thinking through the slowly moving recovery period since the depths of the depression of the early nineteen thirties must also be adjusted—if not, in fact, entirely scrapped. With the war but a few weeks old, we already feel the upheaval—rising commodity prices, increasing interest rates, and particularly the mounting market quotations of certain common stocks—the "war babies." Already just over the horizon we hear again the rumble of coming inflation.

There is something strangely familiar in these early signs. It takes us back a quarter of a century to the latter days of 1914 and the years that immediately followed. Will history repeat itself, or will the difference in the present weight and position of the pendulum develop new and unknown adjustments for which we have no empirical formula for comparison?

Truly, the appraiser, who deals with futures, is going to find himself in something of a "spot" in the months or years to come. His beautifully organized files of costs, sales, rentals, and returns will not bring much as *salvage*, which may possibly represent their "highest and best use" from now on. Of course, the pessimist might suggest that there was no particular reason to lock them up at night even before this war thing started—but that is hardly a fair estimate. As a matter of fact, these data files, developed largely during the past few years, are indexed on a rather flexible system. They bear little resemblance to the newspaper "morgue." The factual information is mobile and designed to disclose relationships that assist in forecasting human behavior under differing sets of circumstances. Anyhow, the system will soon be put to the acid test—and it had better be good!

Looking back to 1914, the costs of construction were virtually at the lowest point of the five-year period prior thereto. The Interstate Commerce Commission, in the valuation of the railroads, adopted June 30, 1914, as a base or "norm" for all subsequent work, developing unit prices on the prior four-year average that approximated the "spot" prices as of that date. The Bureau of Internal Revenue adopted March 1, 1913, as the basic date in all income-tax computations and still adheres to the viewpoint that such was the date of the pre-World War "normal."

Now, what happened after 1914 when Europe went to war? First, construction decreased temporarily because of the rising commodity prices. Then, with the general business increase brought on by the mounting foreign requirements for domestic products of all kinds, an accelerating purchasing power resulted in a real estate demand that very soon turned into a "boom" upon a national scale. Land values — or prices, at least — pyramided overnight, especially in the industrial centers. This was apparently justified by or caused by (as the case may be) rising rents, and of course higher construction costs joined the procession. In spite of this, construction expanded both in industry and home building—and to some lesser extent, perhaps, in commercial building.

With the entrance of the United States into the war in 1917, construction fell off with the need of concentration on war supplies. However, the real "boom" got under way after the Armistice, and by June, 1920, construction costs mounted to the highest level of the century, the index being more than double that of 1914. It is also interesting to observe that farm-land values (or prices) also pyramided until farms in the "corn belt," for example, were selling at prices far in excess of any possible returns from the crop potentialities. Of the later "dip" in 1921, the unprecedented rise thereafter culminating in 1929, and the subsequent depression, nothing need be said here.

The question is, to what extent will history repeat itself, and what may be anticipated—at least in the immediate future—from the present European war? To begin with, the situation is basically different. Construction costs are as high or higher than they have ever been. Labor is in the saddle now and is organized to drive a hard bargain. It is difficult to conceive that rentals, which are still far less than is essential to justify new capital in construction, can rise rapidly enough to satisfy a still further increase in construction costs. And yet, material costs are certain to rise with other commodities, and labor is not going to permit the lowering of wages.

Rentals will certainly rise as the ability to pay increases with expanding employment. This should increase improved real estate values. Interest rates will also rise, however, which will affect capitalization rates and hence offset, at least to some extent, the effect of rental increases. Vacant land would presumably be least affected, since increasing capital investment in improvements at higher interest rates must first be satisfied before residual income would be imputable to land. These and many other things may happen—but will they?

The real estate appraiser must analyze all of these opposing forces, form his conclusions intelligently and conscientiously, and weigh them in his valuation of the future. He should not be led astray by newspaper commentators nor by the wishful thinking of his clients. He will be forced, for a time at least, to look to the experiences of the past. In so doing, however, he will do well to stick closely to the fundamental relationships of cost and value, supply and demand, income and expense, remembering the while the lessons which he has learned by the hard labor of the past few years.

The M.A.I. has already attained a real measure of recognition in his chosen field. He now faces possible economic adjustments, the results of which no one can forecast. The "voice of experience" should be of real assistance in the endeavor, but its words cannot be accepted verbatim. They must be interpreted without hysteria and applied in broad principles only to what appears to be a new set of circumstances.

•

PHYSICAL VALUE

FREQUENTLY, in publications of various sorts, and even in articles in The Appraisal Journal, writers speak of "physical value." From the point of view of the appraiser the two words in combination present what might be called a solecism, provided the word "value" is understood to relate to some amount in dollars which represents the worth of benefits derivable through ownership.

Thinkers in the appraisal field have long realized that, while the dollar amounts of reasonable valuations depend in part upon intrinsic and inherent qualities of the physical objects which are being appraised, nevertheless the dollar values of such things are not intrinsic but are, rather, extrinsic, existing as conceptions in the minds of persons who would be benefited by owning the properties. Certainly a thing of the mind cannot be considered physical.

When appraisers use the term "physical value," they are referring to either the cost of replacing the property under consideration or this cost minus an amount representative of "depreciation," the "depreciation" being calculated with reference to the replacement cost rather than the value new or the value at the time of the appraisal.

The figure derived by this type of procedure is usually contrasted with another figure called the "economic value," which is a figure resulting from consideration of the prospective earning capacity of the property. Frequently a third comparison is made with another figure which is variously designated by use of such terms as market value, market price, comparative-approach estimate, and so on.

The truth is that all value is and must be an economic phenomenon inasmuch as value can exist only in conjunction with the satisfaction of the needs and requirements of mankind. "Economic," of course, relates to the satisfaction of these needs and requirements.

What, then, becomes of the term "physical value" since value is not physical? Obviously it implies a confusion between cost and value, and, since appraisers are endeavoring to promote public understanding of the distinction drawn between these two words, they would do well to abandon a term which tends to perpetuate a misconception regarding them. Perhaps "directly estimated unamortized cost" more truly describes the concept back of the term.

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GROSS INCOME ESTIMATES IN THE VALUATION OF STORES

WALTER R. KUEHNLE, M.A.I.

IN THE appraisal of store properties, accuracy in estimating the gross income is of the utmost importance. An error of 20 per cent in estimating gross income may mean an error of 100 per cent in the valuation. For example, if the effective gross income on a property is $8,000 and the expenses are $6,000, the net income is $2,000. A gross income of around $10,000 with the same expenses returns a net income of $4,000 and, at the same rate of capitalization, results in a valuation twice as great.

The appraisal student is taught that, in order to make an appraisal of an income property, he must determine to the best of his knowledge the gross income that a fully qualified and experienced buyer would feel justified in assuming the property can produce in the future.

The appraiser must, first of all, consider the vacancy or occupancy of each store in the property he is appraising. If a store is vacant, it is necessary to make an estimate of the probable rental the store will produce when and if rented. If it is occupied, the appraiser must analyze the rental which it is producing; he must check the adequacy, justification, security, and duration of the rental. The rental being paid may be too little, or it may be too much; the store may be efficiently or inefficiently utilized; the existing lease may be well secured with a responsible lessee, it may be poorly secured, or it may be entirely unsecured; the present occupancy may be upon a month-to-month basis or it may be for a long term of years. When an estimate of future gross income from such stores is to be used in the appraisal process, it must be based upon the probable future earnings of these stores.

It is therefore apparent that the present rental as shown by the last monthly or yearly statement does not necessarily indicate the future rental. Past income has no significance or meaning other than as an indication of what might happen in the future. The appraiser must analyze the degree to which the existing occupancy, with the rental it produces, utilizes the present possibilities of the premises. He must analyze the responsibility of the tenant, and he must find out the terms of the lease under which the tenant holds possession—its security, justification, and adequacy. In this way, the appraiser ultimately arrives at an informed opinion of the probable future gross income for the stores in the building being appraised.

Gross income from store rentals received from tenants for the right to occupy space in a building may be augmented by additional miscellaneous revenue, such as rental from signs and profit from the sale of electricity to tenants. Care should be taken in including such miscellaneous revenue in the estimated gross income. In many cases, such income is less certain than the regular rentals, and this must be considered when estimating the vacancy and collection-loss allowance.

Highest and best use of an improved property may be defined as that utilization which produces the highest net income and the highest present value. It is apparent, therefore, that the use which produces the highest gross income is not necessarily the highest and best use of the property. The amount of expenses and certainty of the income under various uses must also be considered in determining what program of utilization represents the highest and best use.

FACTORS DETERMINING THE VOLUME OF GROSS INCOME

In determining the stabilized gross income of store properties, the leases and the rental value of the space must be carefully analyzed. The rentals stipulated in the leases and their expiration dates are extremely important. If space is under lease for a definite future period, the estimated gross income for that period cannot exceed the rental stipulated in the lease even though the current rental value of the space is much greater. On the other hand, the lease may call for a rental in excess of the rental value of the space, in which case the excess rental for the period of the lease must be taken into consideration in estimating the future gross income.

In the absence of long-term leases, the appraiser must base his estimate of future gross income upon his opinion of the rental value of the space. He should arrive at such opinion by analyzing actual rentals in the area and comparing them with the space he is appraising. He must ascertain the dates when the existing leases on these other stores were executed, the volume of business done by the stores, if possible, and whether the volume of business being done justifies the rentals paid. He must determine the vacant space available in the area and the average duration of vacancies. Also, if possible, he should determine the volume of business done by the stores in the property he is appraising and the desirability and demand for this particular type of space. With all this information at his command, the appraiser is in a position to determine the rental value of the space.

The terms of leases have a great bearing on the stability of the gross income. For example, if space is rented on a long-term lease at about one half of what the appraiser believes to be the current rental value, it is apparent that the rental received in the lease is highly stable. On the other hand, a long-term lease calling for a rental in excess of the current rental value of the space to a tenant whose financial position is not strong or who is paying unwillingly must be regarded as uncertain and must be discounted in accordance with the facts in determining the stabilized gross income. Stability of income based upon month-to-month or year-to-year leases depends largely on the space itself, the amount of business done, the appropriateness of the use, and trends in the development of the neighborhood and the city.

TYPES OF LEASES

Month-to-month occupancy extends from month to month at the same rental until either party gives notice of his desire to terminate the occupancy. Such tenancy may or may not be under a written lease.

A short-term lease, which may be for a term of a year or several years, calls for a certain specified rental to be paid at specified periods. When these leases are for more than one year, they sometimes call for a graduated rental, increasing or decreasing in the subsequent years of the lease.

Long-term leases may vary from a ten-year lease on a store to a ninety-nine-year or longer lease on an entire property. This type of lease may call for a level rental throughout the term or may call for a graduated rental, increasing or decreasing in subsequent years. A store lease, where the tenant leases only part of the premises, will seldom exceed twenty-five years, and in most cases it does not exceed ten to fifteen years. Usually, ninety-nine-year leases are ground leases where the tenant builds his own building and pays the expenses, including taxes.

A real estate reappraisement lease calls for a reappraisal at fixed periods during its term, such as every five or ten years, at which time the appraisers, who are appointed under provisions in the lease, determine the new rental.

A percentage lease may be either a straight percentage lease or a percentage lease with a minimum-rental provision. A straight percentage lease calls for a stated percentage of the volume of business done. A percentage lease with a minimum-rental clause is the same as a straight percentage lease with the exception that a fixed rental payable at specified periods is provided for, regardless of the volume of business actually done on the premises. (A percentage lease may be based upon more than one percentage, the percentage varying as increasing business volumes are reached.)

BASIC TYPES OF RETAIL DISTRICTS

Neighborhood locations: In neighborhood locations the merchant depends on his immediately surrounding area for his patronage. Food and service stores are the predominant retail establishments in the neighborhood business district, but such a district may vary from a well-developed district, consisting of meat markets, grocery, drug, and vegetable stores, five-and-ten-cent stores, and a movie theatre, down to a small business corner consisting of a grocery store and meat market. The size and type of the retail establishments in the area will depend on the type and number of the immediately surrounding population and the proximity of other business areas. Proximity to an outlying business center will restrict the development of a neighborhood business district. A business district located in the center of an intensively developed apartment section will naturally be more successful than a business district serving an area of single-family dwellings.

Main thoroughfares: Retail utilization may extend through entire cities from one end to the other along a main streetcar line or a main thoroughfare. The type of utilization found in the various sections of the thoroughfare may vary according to the district through which it passes. Consequently, such a street has many types of business locations, varying from the poorest type of neighborhood locations to primary outlying business-district locations. Anything from gas stations, printing shops, lunchrooms, and tinsmiths to automobile salesrooms and department stores may be found in the length of such a street. Accordingly, the character of the main thoroughfare as a business street cannot be definitely defined except as a series of various types of business sections.

Satellite locations: In satellite locations the merchant depends on the patrons of an adjoining attraction, such as a theatre, stadium, etc. Popcorn shops, candy stores, ice-cream parlors, restaurants, taverns, etc. represent typical uses of these locations.

Outlying business centers: The primary outlying business center is a reproduction on a smaller scale of the central business district. It may be either primary or secondary. In the primary districts in the large cities will be found practically every type of business, including most of the large chain stores and sometimes branches of the large department stores represented in the central business district, which have located there because of closer proximity to their patrons and better automobile parking facilities. In the secondary centers, the stores will be less elaborate and the selection of merchandise less representative. These are generally districts that aspired to primary importance, but did not have the necessary factors to a sufficiently intensive degree.

Central business district: The central business district is the retail and financial center of the city. Such a district serves the retail needs of the entire city. Large department stores and chain stores dominate its shopping streets. Direct, good transportation to all parts of the city and a lack of free parking space for automobiles are among the characteristics of such a district. It is considered the highest type of business district. A study of the sales of merchants in the central business district of large cities shows a pronounced falling off of business in that district coincidental with continued growth of the primary outlying retail districts. The large retail chains and merchants have taken their wares to the consumer in outlying districts, with the result that it is no longer as important for the consumer to go to the central business district. Consequently, much business that was formerly transacted in the central business district is now transacted in outlying business centers. This shift of concentration in retail purchasing has been called decentralization.

The complexity of forecasting the probable future rental figure increases as we progress from the neighborhood location to the central business district. Let us examine the forces behind each of these five types of locations. The determining element is purchasing power. The amount of rent a merchant can pay is limited by one thing: the profitable volume of gross business that can be done at the location. The possible purchasing power is the factor that gives a store a rental value. If the little candy store across the street from the grammar school commands a rental of only $10 per month, that is because it has only a limited number of patrons, and they are customers who deal in pennies instead of dollars. At the other extreme, we have the central-business-district store serving a large number of patrons who contribute a very large gross volume of business.

In the following pages are described more fully each of the five groups of business property and the influences surrounding the inherent rental value of each.

ECONOMIC FACTORS IN RETAIL-STORE RENTALS

Although the importance of location in retailing is fundamental, the maximum amount of business that can be done on any site, and consequently the amount of rent which the tenant can pay, is limited by three major factors, as follows:

1. The total income of the potential customers.
2. The amount of this income which they can or will spend for the particular kind and quality of merchandise sold by the tenant.
3. The existing competition for this trade.

Coincidental with the shrinkage of our national income, there has been a shrinkage in the volume of retail sales. This shrinkage, although experienced by most lines of business, has been most severe in the higher-priced merchandise and luxury lines. During the depression, business streets devoted to class instead of mass trade practically went out of business, and owners were carrying tenants who could not pay. In such times the public becomes very keen on price and value differences, and profit margins are reduced by keen competition. It is apparent, therefore, that the trend of general economic conditions has an important effect on the sales volume and profit of the tenant, and this in turn is reflected in the rental value of the retail store.

The growth of competing retail business areas is, however, another factor affecting future rental value. The decentralization of concentrated shopping from the central business district to outlying business centers is an excellent example of this point. The effect of competing retail business areas on the future rental value of central-business-district sites will be governed by the extent that these competing retail business sections attract a portion of the total available business formerly done in the central business district.

The retail trade figures made available by the United States Department of Commerce and presented here in Figures I and II are estimates of the Marketing Research Division, Bureau of Foreign and Domestic Commerce, and actual census figures reported by the Bureau of the Census. The estimated group totals (Figure I) are arrived at by building up separately the sales of the different kinds of stores included in each business classification and are tied in with the actual census figures. The total sales figures are obtained by adding the estimated figures for each business group. In determining the trend and amount of change in the different kinds of business represented, an analysis of numerous data was made which included retail figures on independent chain-store activity reported to the Marketing Research Division and various series relative to trade, production, consumption, and prices collected by other governmental and nongovernmental agencies. Although the final estimates may differ only slightly from the preliminary figures, due consideration is given to year-end material which becomes available after the preliminary estimates are published.

GROSS INCOME OF STORES IN NEIGHBORHOOD LOCATIONS

In analyzing gross income in any type of store property, the appraiser must always keep purchasing power in mind and remember that the rental value of a store can be little greater than the ability of the tenant to make a profit. The method of subdividing some of our cities, with half-section and section lines allotted and zoned for business, has produced an excess of business property. Business streets that are solidly backed with apartment buildings giving a large supporting population within a very short radius are usually more prosperous than business streets supported by residences. An exception to this will be found in certain districts where most of the shopping is done in neighborhood locations because the local "language" is spoken by storekeepers. The presence of competing business streets, railroad embankments, or wide streets with heavy traffic often cuts off one half or at least a portion of the area in the radius of probable patronage, thus affecting the prosperity of retail business streets. Also detrimental to retail stores is proximity to undertaking establishments, storage buildings, vacant stores, dilapidated and unsightly structures, or a break in shopping continuity caused by the presence of bank buildings or other institutional buildings. Streets on which the shopping continuity is broken by short blocks and alleys are greatly handicapped.

In making a gross income analysis and estimate for stores in neighborhood locations, the appraiser's data on the existing store rentals will very likely be patterned along the lines indicated in the tabulation shown on page 312.

Store No. 1, the tavern, has an option for two additional years at $175 per month. In connection with Store No. 4, the bakery, a new addition has been built at the rear,

ESTIMATED NET SALES OF RETAILERS, BY KIND OF BUSINESS, 1929-1938, INCLUSIVE[1]

KIND OF BUSINESS[2]	1938 Est.		SALES IN MILLIONS OF DOLLARS										PERCENTAGE OF 1929 (1929=100)									
	Per cent change from 1937	Percentage of total sales	1938 Est.	1937 Est.	1936 Est.	1935 Act.	1934 Est.	1933 Act.	1932 Est.	1931 Est.	1930 Est.	1929 Act.	1938 Est.	1937 Est.	1936 Est.	1935 Act.	1934 Est.	1933 Act.	1932 Est.	1931 Est.	1930 Est.	1929 Act.
Total	-11.3	100.0	35,425	39,930	37,940	33,161	29,188	25,037	25,597	35,414	42,849	49,115	72	81	77	68	59	51	52	72	87	100.0
Food group[3]	– 4.5	25.4	8,920	9,340	8,981	8,362	7,580	6,776	7,261	8,994	10,287	10,837	82	86	83	77	70	63	67	83	95	100.0
Beer & liquor stores	– 3.5	1.1	394	408	394	328	260	17	......	......	......	......	....	....	....	....	....	....	....	....	....	......
Eating & drinking places	– 7.0	7.5	2,676	2,878	2,702	2,391	1,932	1,430	1,636	1,934	2,061	2,125	126	135	127	113	91	67	77	91	97	100.0
Farmers' supply & gen. stores[3]	-10.5	5.0	1,784	1,993	1,898	1,710	1,665	1,561	1,218	2,028	2,830	3,690	48	54	51	46	45	42	33	55	77	100.0
Dept., dry goods, & gen. mdse.	– 8.0	10.7	3,783	4,107	3,874	3,453	3,280	2,993	3,208	4,176	4,685	5,093	74	81	76	68	64	59	63	82	92	100.0
Mail order (catalogue sales of general mdse. stores)	– 5.5	1.3	463	490	460	386	300	220	201	259	349	447	104	110	103	86	67	49	45	58	78	100.0
Variety stores	– 3.0	2.4	858	885	851	781	754	678	660	787	832	904	95	98	94	86	83	75	73	87	92	100.0
Apparel group	– 8.5	8.2	2,923	3,195	3,028	2,656	2,372	1,923	2,331	3,496	3,920	4,241	69	75	71	63	56	45	55	82	92	100.0
Automotive group	-34.0	11.0	3,900	5,910	5,711	4,606	3,559	2,887	2,178	4,173	5,535	7,829	50	75	73	59	45	37	28	53	71	100.0
Filling stations	– 3.0	6.8	2,404	2,478	2,263	1,968	1,750	1,532	1,665	1,827	2,265	1,787	135	139	127	110	98	86	93	102	127	100.0
Furniture & household	-17.0	4.0	1,425	1,718	1,613	1,290	1,092	959	895	1,618	2,200	2,755	52	63	59	47	40	35	32	59	80	100.0
Lumber, building, & hardware	-11.5	6.4	2,270	2,565	2,375	1,864	1,550	1,343	1,389	2,006	3,110	3,846	59	67	62	48	40	35	36	52	81	100.0
Drugstores	– 2.5	3.9	1,376	1,411	1,344	1,233	1,156	1,066	1,182	1,438	1,554	1,690	81	84	80	73	68	63	70	85	92	100.0
Jewelry stores	-10.5	.8	279	312	282	235	203	175	188	301	381	536	52	58	53	44	38	33	35	56	71	100.0
Other stores	-12.0	5.5	1,970	2,240	2,164	1,898	1,735	1,477	1,585	2,377	2,840	3,335	59	67	65	57	52	44	48	71	85	100.0

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[1] Estimates are by the Bureau of Foreign and Domestic Commerce based on trends indicated by currently published statistics and are tied in with the actual census figures as published by the Bureau of the Census for 1929, 1933, and 1935 which are shown herewith.

[2] Commodity groups include kinds of business as shown in the 1935 Census of Business.

[3] The 1935 census includes in the food group some stores classified as country general stores in the two previous censuses. Classifications in 1935 were based more strictly on a commodity basis. The inclusion of additional commodity information and other descriptive characteristics asked for in the 1935 schedules permitted more accurate classifications than were previously possible. Hence, country general stores with food sales amounting to over half of total store sales were put in the food group. Sales figures for the two groups after adjustments for changes in classifications for the years 1929-1934, inclusive, are estimated as follows and include recent slight revisions:

	1938	1937	1936	1935	1934	1933	1932	1931	1930	1929
Food group (millions)	$8,920	$9,340	$8,981	$8,362	$7,734	$7,086	$7,506	$9,385	$10,811	$11,501
Percentage of 1929	77	81	78	73	67	62	65	82	94	100
Farmers' & general stores (millions)	$1,784	$1,993	$1,898	$1,710	$1,511	$1,251	$ 973	$1,637	$ 2,306	$ 3,026
Percentage of 1929	59	66	63	57	50	41	32	54	76	100

Prepared in the Market Data Section, Marketing Research Division, Bureau of Foreign and Domestic Commerce, Department of Commerce.

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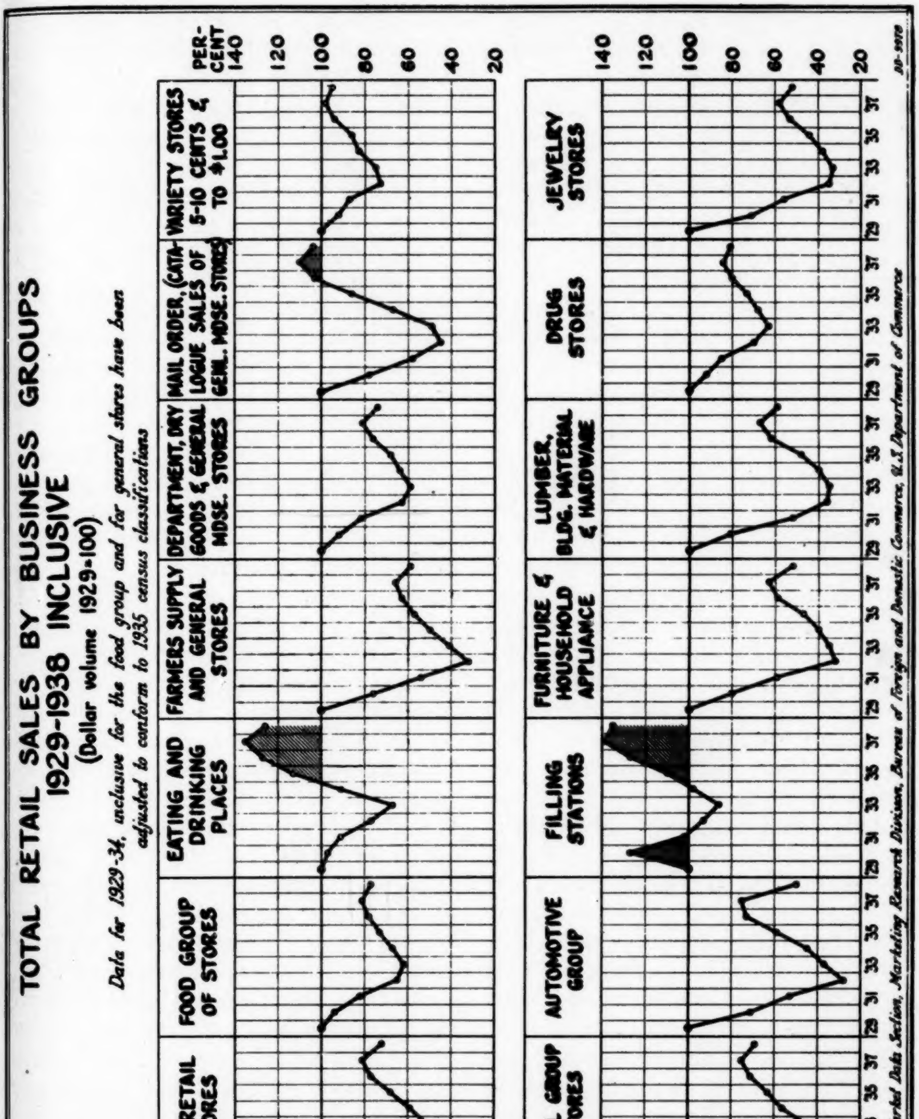
FIGURE I



Prepared in the Market Data Section, Marketing Research Division, Bureau of Foreign and Domestic Commerce, U.S. Department of Commerce

Figure II

STORE RENTALS AND LEASES
(as of August 1, 1935)
Three-Story Brick Store and Apartment Building
N. E. Corner 82nd Street and Ellis Avenue, Chicago, Illinois

Store No.	Address	Business	Frontage (Feet)	Area (Square Feet)	Period of Lease	Monthly Rental
1	1000 E. 82nd St.	Tavern	20	1,200	3/1/34— 2/29/36	$150
2	1002 E. 82nd St.	Grocery	14	840	2/1/34— 1/31/36	$ 85
3	1004 E. 82nd St.	Meat market	16	960	11/1/33—10/31/36	$100
4	1006 E. 82nd St.	Bakery	17	1,350	12/1/32—11/30/37	$ 90
5	1008 E. 82nd St.	Barbershop	17	1,020	10/1/34— 9/30/35	$ 90
6	1010 E. 82nd St.	Shoe-repair shop	14	840	11/1/34—10/31/35	$ 90
7	1010½ E. 82nd St.	Jewelery	11	649	6/1/31— 5/31/36	$ 55
8	1012 E. 82nd St.	Confectionery	14	784	6/1/31— 5/31/36	$ 90

increasing the area, and a new lease signed running from December 1, 1935, to November 30, 1940, at $125 per month. The tenant in Store No. 5, the barbershop, has an option for two additional years at $100 per month.

With the present rental schedule of the stores before the appraiser, his next step is to analyze the adequacy of the occupancies, the present rentals, and their conformance with the neighborhood level, together with the probable future trend of these rentals and the indicated security for continuance of the present tenant—a factor generally measured by the tenant's success in his business enterprise.

In making this analysis, the appraiser must first determine the relative business importance, as store locations, of the stores analyzed compared with other stores serving the same area. Then he must study and analyze prevailing rentals on other stores in the locality and judge their comparative significance in determining proper store rentals for the property being appraised.

In the case of the section in which the subject building is located, the property west of the Illinois Central Railroad on 82nd Street divides itself into two groups—the store locations on the south and those on the north side of the street. Of the two, those on the south side of the street obviously command the greater purchasing power and rental value.

Merchants probably found the south side of the street better from the beginning because of the greater traffic resulting from the entrance there to the Illinois Central suburban station. The entire south side of the street is one long unbroken block from Ellis Avenue to the Illinois Central station. As the Illinois Central suburban service is the most important and intensively used transportation to this area, these stores supplying daily necessities are fortunately located for convenience. As a result, all of the more successful merchants and the chain-store organizations have consistently resisted attempts to lure their existing stores to the north side of the street. Similar attempts to attract new chain-store organizations not represented in the district to stores on the north side of the street have failed.

Although this business section is rather intensively developed, it has definite limitations because it serves only a local community and because apparently the south side of the street affords all the space required for chain stores and other higher-caliber tenancies. Also, strong nonchain-store tenants will naturally group around the chains. Stores on the north side of the street do a certain amount of business but less than those on the other side. They therefore have less rent-paying ability.

Another factor handicapping the north side of the street is lack of continuity of store space. It is improved westward from the railroad with a service station which extends to the corner of Dobson Avenue, and Dobson Avenue itself interrupts the continuity of business. From Dobson Avenue west to Ellis Avenue, 82nd Street is improved with two three-story store and apartment buildings. One of these buildings occupies the corner of Dobson Avenue to the alley, and the other is the property being appraised, which occupies the land from the alley west to Ellis Avenue, the western boundary of the present business area and zoning. The tenants in these two buildings, which contain the only stores on the north side of the street, do not get as much business as the tenants on the south side of the street.

Summarized, the occupancy of the north and south sides of 82nd Street from the Illinois Central structure to Ellis Avenue appeared on September 1, 1935, as follows:

NORTH SIDE

Gas station
Dobson Avenue
Cleaning shop
Gift shop
Lingerie shop
Laundry
Delicatessen
Tailor shop
Radio-service store
Barbershop
Alley
Confectionery
Jewelry
Shoe-repair shop
Barbershop
Bakery
Meat market
Grocery
Tavern (N.E. Corner 82nd St.)

SOUTH SIDE

Independent drugstore
Dutch Mill candy chain store
Tailor shop
Atlantic & Pacific Tea Company
Bakery
Kroger-Consumers
Dry-goods store
Meat market
Vegetables and meats
National Tea Company
Beauty shop
Alley
Fruit store
Meat market
Delicatessen
Cleaning shop
Cushman bakery
Restaurant
Walgreen chain drugstore (S.E. Cor. 82nd St.)

A glance at the above list of tenancies immediately illustrates the superiority of the south side of the street.

For the reasons cited, attempts in the past to maintain a rental schedule on the north side of the street consistent with that on the opposite side of the street have resulted in the failure of the tenants who attempted to pay such rentals. The owner was finally obliged to accept a rental reconcilable with the business that could be transacted in the store.

Having analyzed the present use and the present relationships of the various properties within a district, it is necessary for the appraiser to study the probable trend of the district as a whole. A dwindling supporting population in certain old sections caused by the restriction of immigration to the United States, coupled with the tendency of succeeding generations to become Americanized and move away from foreign districts to newer and more pleasant neighborhoods, is resulting in a steady decline in the business property supported by these districts. The infiltration of inharmonious uses may also bring about a decline in business property. In certain sections adjacent to newer areas where supporting population is increasing, the trend generally is upward. It is therefore very important, in estimating a future store rental, for the appraiser to arrive at an opinion as to whether the district is improving, declining, or static. He must be alert to the fact that where new, potential business sections exist, they may grow to pull purchasing power away from the district in which the property appraised is located.

In the case of the property under consideration, the business section is a small but intensive one which owes its existence to a combination of artificial restrictions and natural advantages. The artificial restrictions are zoning, which limits business frontage to about one full block, and the fact that the present costly three-story apartment buildings on the business street (82nd Street) to the west of the present business limits (both by zoning and by use) make it highly improbable that any attempt will be made to extend this business street to the west.

The area to the east of the Illinois Central embankment, in which several large industrial tracts are located, is restricted largely to single-family dwellings which at the present time are mostly vacant. Attempts have been made to improve 82nd Street east of the Illinois Central embankment with apartment buildings, some of which have basement stores and some of which have regular first-floor store space. At the present time these stores are either vacant or give the appearance of definite absence of prosperity. Rentals being paid by tenants for these stores average $30 per month per store.

The natural advantages of this business district lie in its heavily populated supporting area, rather solidly built up with three-story walk-up apartments (the average age of these buildings being ten to fifteen years), and the presence of the 82nd Street station of the Illinois Central Railroad. Because the railroad is the principal transportation of the district, a majority of the residents of the area pass through this business district frequently. At this time it does not seem that the present or potential competition of any other business streets touching the borders of this area will be able to affect the concentration of purchasing power enjoyed by this little business district.

A study of the situation leads to the logical conclusion that (1) these stores are located in a monopolistic neighborhood business district which is well supported by a well-populated apartment-building area and that (2) this business district will continue to serve the area.

The advantage of the Illinois Central station, which forms the hub of the district, lends a monopolistic advantage which seems to indicate stability for the future. The railroad station entrance and the long block unbroken by cross streets are additional factors contributing to this stability. The appraiser realizes that the higher rentals prevailing just a few feet away from the property appraised are like the "grapes of Tantalus" to the owner of the less fortunate locations; but he also knows that merchants succeed or fail as their locations are favorable or unfavorable. He also knows that attempts to secure a substantially higher rental than that prevailing has resulted in the failure of former tenants of these stores *because the tenants could not transact as great a volume of business in these stores as was done by the more advantageously located stores on the south side of the street.*

Accordingly, the appraiser ignores these higher rentals being obtained across the street. He realizes that they have no significance in so far as the stores under consideration are concerned. Had this differential in rents been attributable to poor management or to old leases made when lower rentals prevailed, it would be proper for the appraiser to adjust his estimate of the future rentals in the appraised property to a correct level as of the time that the existing leases expired. The appraiser must always assume that competent management will put the property to its most productive use at the expiration of existing lease contracts.

After the appraiser has carefully considered the future of this business district and the relative rental value of the stores appraised compared with all others within the boundaries of the business district, he turns his attention back to the present rentals being paid by the existing store tenants.

An investigation of Store No. 1 (the tavern) seems to indicate that this enterprise has reached a degree of success that will cause the tenant to exercise the option at $175 per month for two years. At the end of that time, it is estimated that a higher rental may be obtained, which for the sake of conservatism is estimated at $180.

The bakery, Store No. 4, has occupied its present location for some time, and the tenant has signed a new lease for $125 per month for his old space, together with the new addition in the rear.

All of the stores seem to be doing business commensurate with their location, and, with some improvement of business conditions during the next five years, slightly increasing rentals could reasonably be anticipated. In fact, slightly higher rentals might already have been in effect had it not been for the unsuccessful attempts to match rentals on the south side of the street.

After consideration of all the information he has acquired, the appraiser again consults his schedule of present rentals. The following estimate represents the attempt of the writer, when making his August 1, 1935, valuation of this property, to estimate the probable future rental of these stores upon a conservative basis. As estimated in the appraisal made in 1935, five years were required to bring the store rentals to normal on the property under consideration.

PRESENT RENTALS AND FUTURE ESTIMATED RENTALS OF STORES
N. E. Corner 82nd Street and Ellis Avenue, Chicago, Illinois

Occupant	No.	Frontage (Feet)	Lease Expiration Mo., Day, Yr.	Present Rental	First Year	Second Year	Third Year	Fourth Year	Fifth Year
Tavern	1	20	2-29-36	$150	$155	$165	$175	$175	$180
Grocery	2	14	1-31-36	$ 85	$ 95	$100	$105	$105	$110
Meat market	3	16	10-31-36	$100	$100	$105	$110	$110	$115
Bakery	4	17	11-30-37	$ 90	$120	$125	$125	$125	$130
Barbershop	5	17	9-30-35	$ 90	$100	$100	$115	$115	$120
Shoe-repair shop	6	14	10-31-35	$ 90	$ 95	$100	$105	$105	$110
Jewelry	7	11	5-31-36	$ 55	$ 55	$ 60	$ 60	$ 60	$ 65
Confectionery	8	14	5-31-36	$ 90	$ 95	$100	$105	$105	$110
Total—Stores per month				$750	$815	$855	$900	$900	$940
Total—Stores per annum				$9,000	$9,780	$10,260	$10,800	$10,800	$11,280

The following footnote was included in the appraisal regarding the above estimate:

> No claim is made of accurately predicting the exact future income of each store. The above detailed figures are merely the basis of an estimate of the future probable gross income, before vacancy or collection losses on the stores, to bring the store rentals to their normal over the period of the next five years. Beyond this period it is very difficult to estimate, and the appraiser can only assume that having attained normal, they will remain there. It must be remembered that the appraiser is here making such assumptions as a prudent buyer would be justified in making at the time of the appraisal.

As the buyer of income property is interested primarily in the future income which the property will produce, the price he will pay will be definitely affected by his present judgment as to the probable amount of that future income. Subsequent changing economic conditions not apparent at the time of the appraisal may cause the income to be far different from the estimate made by a prudent, well-informed buyer. If such influences did not seem probable at the time the value estimate was made, the appraiser could not be expected to have reflected them in his judgment. On the other hand, potential possibilities of income decreases or increases may be evident at the time of the value estimate, and the appraiser should reflect them conservatively in his valuation.

The preceding 1935 estimate of future store-rental income on the 82nd Street property is selected as an example because it enables the writer to point out both the mechanics and the objective of future rental estimation by a comparison of an actual store-rental estimate with the rental actually produced by these same stores during the period covered by the estimate. A reinvestigation made by the writer on the rental schedule in effect on these stores on September 9, 1937 (during the second year of the estimate), revealed the stores to be upon a basis of $10,900, as compared with the appraiser's estimate of $10,260 made on August 1, 1935. On June 3, 1939 (during the fourth year of the estimate), the writer again investigated the rental schedule of these stores. He found it to be upon an annual basis of $12,364, as compared with the estimate made in 1935 of $10,800 for the fourth year and a normal of $11,280 at the fifth year.

As of June, 1939, changes from the 1935 tenancy had occurred as follows: Store No. 2 was a beauty shop; Store No. 3, a liquor store; and Store No. 7, a notion store.

Accordingly this estimate of future increased store rentals made in 1935 now appears to have been fully justified.

This comparison between a 1935 estimate of future store rentals with the rentals actually obtained during the period covered by the estimate illustrates that existing store rentals do not necessarily represent the probable future store rentals. Each case must stand on its own facts.

GROSS INCOME OF STORES ON MAIN THOROUGHFARES

A main thoroughfare may continue as a business street through a city from limit to limit. It may include many types of business sites. Throughout the length of the main street a core is formed for various types of residential areas, and varying classes of outlying business districts appear. At strategic points, primary nucleations occur. In other sections along its length the street passes through close-in, old sections with little purchasing power available in the territory immediately surrounding them. In such cases, if the street should be a main automobile artery, business districts devoted to automobile salesrooms and automobile-accessory stores may develop. In estimating income of stores on such a street, the appraiser must of course analyze the particular section of the street in which the property to be appraised is located. The procedure of estimating the gross income will in general be similar to that described here for the various definite types of retail business locations.

GROSS INCOME OF STORES IN SATELLITE LOCATIONS

Satellite locations are generally stable for certain lines of business that are in agreement with the character of the primary development as long as the attraction which they adjoin remains in operation and does not make radical changes in operating policy or suffer a decline. In analyzing store rentals on this type of property, it must be remembered that the people attracted to such a location do not come for the purpose of shopping. Therefore, businesses that are most likely to operate successfully in such a location are those that furnish certain conveniences appurtenant to the primary development. When the purpose of such a primary development is some form of entertainment or amusement, the corollary businesses may be candy and popcorn stores, restaurants, ice-cream parlors, taverns, etc.

During the building boom of the twenties, the announcement that a new motion-picture theatre was to be built in a block brought a frenzy of speculation in adjacent land on the theory that a tremendous retail value would be developed as a result of the great number of people to be attracted. Time and experience have proved the fallacy of this reasoning. Although the number of people who pass a store is important, *why* they pass is also vitally important. Theatre patrons come with the purpose of seeing the show. The majority of them do not care to disturb this objective by shopping; their time is limited, and they do not wish to be bothered with packages. Consequently, dress shops, hat stores, haberdasheries, etc. which were located around theatres did not do the business expected, and substantial retail rentals were never realized from such stores.

Inspection of several theatre blocks will confirm in the observer's mind the fact that the retail development existing in such locations is almost entirely adjoining the development and does not extend far from it. Also, it will be apparent that this retail development is secondary in character and that the better retail stores avoid these locations.

Information obtained as to the rental schedule for satellite locations will be much the same as that shown in the example for the neighborhood-store location. In analyzing the relative importance of the location of the stores appraised with other store locations in the development, accessibility and convenience to the patrons of the *primary attraction* are of first importance. Proximity to the main entrance of the primary attraction may be the controlling factor. Prosperity of the stores might be greater to the right of the entrance than to the left if, for example, people pass that way to park their cars. Factors such as these determine the relative prosperity of stores in such locations.

The term "satellite development" used in connection with this type of district implies a dependence on the primary project for success. Should the primary attraction fail or decline, the satellite development cannot hope to exist. Therefore, an intelligent estimate of the future of the development can be made only if the appraiser has data and knowledge that will enable him to appraise the future of the primary development. Such knowledge would include facts about the adaptability of the structure to other uses, the degree of efficiency with which the structure serves present-day requirements, the existence of present competing developments, and the comparative degree of efficiency with which they serve the same purpose and market as the development under consideration.

THE PERCENTAGE LEASE

In neighborhood store properties, the so-called percentage lease will be found only in exceptional cases. In this type of store, the landlord and prospective tenant generally arrive at fixed rental terms for a short-term lease which sometimes includes option privileges for an additional term, also at a fixed rental. Such short-term leases, ranging from one to five years, give the landlord and tenant an opportunity to negotiate at the time of expiration if the rental has proved too high or too low. It is up to the tenant to make a success of the business once the lease is made.

Sometimes, because of imagination and initiative, the tenant is able to attract a volume of business not normally possible from the location. An example of such a business would be a well-known sandwich shop or eating place. In other cases, the tenant overestimates the business that he can do at the location, and one of two things happens—the tenant hangs on to his unprofitable location to protect his investment, with himself and members of his family supplying the personnel; or he fails, and the store is again for rent.

It has been stated previously that the amount of rental that a store can pay is limited only by the volume of business that can be done in the store, but the volume of business *does* very definitely limit the rental that can be paid.

When an individual merchant (or a chain-store organization) goes about renting a store in one of these districts, he is entering into an important business transaction. The owner of the property is turning over to the tenant for use a valuable piece of property on which the owner wishes to obtain the maximum inherent return. The tenant, on the other hand, is embarking on a new business enterprise of importance. He must not only pay the rental that he contracts to pay for use of the premises, but he must also make a large investment in fixtures and stock and must assume obligations of operating charges for personnel, light, advertising, etc. Unlike the neighborhood store, this enterprise must be self-supporting; if expenses exceed the amount taken in, the enterprise will either fail or be supported by the tenant's more fortunate ventures.

Large merchandisers have an exact knowledge of their business which enables them to know what percentage of each dollar taken in can be paid for rent. This percentage that can be paid for rent varies with various types of businesses, but, generally speaking, the percentage is high on long-profit merchandise and low on short-profit merchandise. In other words, the store selling $22.50 suits cannot normally pay as large a part of each dollar taken in for rent as the store selling $50.00 suits.

The tenant for one of these more valuable locations generally requires a longer-term lease than the small outlying-store tenant because of larger initial investment. As negotiations continue between the landlord and tenant, they invariably arrive at a point where the landlord is unwilling to tie up the potential possibilities of his property at less than a certain rental, which the tenant in turn feels dubious about being able to pay out of the volume of sales that may be transacted in the prospective store. Furthermore, the landlord realizes that an improvement in business conditions, or such economic fluctuations as inflation, might cause a straight lease to be a handicap to the property. Also, increased operating expenses and increased taxes may cause the property to show a great shrinkage in net income if the gross income is fixed.

The writer remembers a property in the central business district in Chicago where the lessor made a straight lease many years ago under which he agreed to pay the taxes. The taxes subsequently rose to more than the rental under the lease. In such straight leases where the owner pays the taxes, many lessors now cover themselves against such a contingency with a tax-participation clause, whereby the tenant agrees to pay as additional rental any increase in taxes over a certain amount.

Into this breach logically comes what is known as the *percentage lease.* This type of lease generally, but not always, provides that the tenant shall pay a minimum rental. This minimum, established by negotiation between the lessor and lessee, is usually fixed at some point where the tenant will feel safe in assuming a definite rental obligation and the lessor will be covered on his operating expenses, taxes, etc.

The percentage lease fixes a percentage of each gross dollar taken in (before sales tax and after returns) which will be paid to the lessor as rental for the premises. If the percentage of sales is less than the minimum rental, the tenant is nevertheless obliged to pay the minimum rental guaranteed. Some such leases have what is known as a recapture clause by which the lessor reserves the right to terminate the lease at certain dates before its expiration if the sales of the lessee (and the rental paid) have not reached a stated amount. The lessee generally has the right to remain if he pays the difference. The purpose of the clause is to enable the owner to protect himself against a tenant remaining in possession who may be diverting business to another location or who, by inefficient operation, may fail to utilize the full potentialities of the location.

The percentage lease should operate in a satisfactory manner if:

1. The property owner is protected by a minimum guarantee that covers his fixed expenses on the property.
2. The percentage of sales volume provided represents the correct percentage for the business, the merchandise price range, and the location.
3. The tenant has capable management and the necessary capital.
4. The business is suitable to the location and the space fits its requirements.
5. The type of business is not overdone in the location.
6. There is not a probability of excessive future competition materializing in the particular line of business in the vicinity.

Proponents of the percentage lease believe it to be the most logical arrangement because it "renders unto Caesar the things which are Caesar's" and properly assigns the component parts of the site product—the profit from the present and future site characteristics going to the owner of the property and the results of skillful merchandising going to the tenant.

Percentage rentals may vary from 1 per cent of sales volume on foodstuffs up to 15 per cent on ladies' hats. In many such leases, this percentage of sales volume to be paid as rental is on a sliding scale, increasing as the sales volume rises, in recognition of the fact that the lessee's overhead costs on each $1.00 of sales decrease as the sales volume increases. Percentage leases generally give the lessor the right of access to the books of the tenant, who is required to report his sales at regular periods, varying from once a month to once a year. This report is very often in the form of a certificate by a reliable accountant.

Various tables are available which give the percentages of the volume of sales that various businesses can afford to pay for rent. These tables are in general made up by specialists in chain-store leasing and are based upon their experience and upon studies made by business schools and chain-store groups.[1] They generally represent the maximum percentage as will be shown by the actual percentages paid as rental by various kinds of businesses.[2] While these percentages may be very helpful, they must be used with discretion since different localities and conditions may cause the percentages to vary widely. In many cases it is difficult to segregate the item of good will of the tenant, and the appraiser will find that one tenant, because of his own drawing power or an unusual amount of advertising, is doing business out of proportion to the rental value of the space.

TRAFFIC COUNTS

The most desirable location for a retail establishment is one accessible to the greatest number of potential customers. For this reason much time and study have been given to pedestrian traffic counts by both chain-store organizations and real estate men engaged in renting retail stores. It has been established that it is not the quantity of the traffic that brings business to the stores but the buying power and the buying mood of the traffic. A difference in weight is attached to the convenience of locations for the purchase of various articles by various groups, and considerable technique in location analysis has been developed by chain-store organizations in recent years.

In classifying the passing pedestrian traffic, separate counts are made on men, women, and children, and even separate counts on economic groups by point of origin, destination, economic level, social characteristics, motives, and state of mind. Counts are made showing the number per hour for periods ranging from certain hours of the day to the entire day. Comparative counts may be made at various points in the district or in a particular block between the corners and the center of the block. One of the simplest and most effective ways of counting the traffic in a retail block is to place a man at each end of the block to count only the persons *leaving* the block.

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[1] K. Lee Hyder, "Percentage Lease Rates," *The Journal of the American Institute of Real Estate Appraisers*, April, 1934, p. 208; Philip W. Kniskern, *Real Estate Appraisal and Valuation* (New York, The Ronald Press Company, 1933), p. 337.

[2] Carl N. Schmalz, *Operating Results of Department and Specialty Stores, 1937* (Cambridge, Harvard Business Studies, Vol. XXV, No. 3, 1938).

Little importance is now paid to passing automobile traffic on main highways and thoroughfares as a source of business to the average retail business district, but parking facilities and the number of automobiles that park in the district are of great importance.

GROSS INCOME OF STORES IN PRIMARY OUTLYING BUSINESS CENTERS

Most substantial tenants in the primary outlying business districts will be found to have long leases. However, in some instances tenants are in possession of stores under various special arrangements, including stop-gap leases from month to month, year-to-year leases, leases with cancellation clauses at the landlord's option, long-term leases, etc. Ten-year and twenty-year leases are common. Some leases are net, the tenant paying all expenses, taxes, insurance, operating costs, etc., whereas in others the landlord pays all expenses. Some tenants in these districts rent only stores; others rent stores including the basement and second floor; and some rent whole buildings, ranging from small retail stores to huge department stores.

In some cases the landlord furnishes the improvements; in other cases the tenant remodels or builds at his own expense. Some occupants own their own property. Terms of leases cannot be considered standard except for the amount of rent. The terms of the more important leases will be found as broad in their differences as the entire field of contractual relations. Obviously, in estimating the adequacy of the existing rental on such a property and making comparisons with other rentals obtaining in the area, the appraiser must have an understanding of the terms of the leases under which the rentals he is considering are paid so that he may reduce them all to a common denominator.

A statement of the volume of business done at any location is essential to the appraiser in arriving at an informed conclusion regarding its rental value. Here, as in the neighborhood location, the question of comparison is also important. Just as the location of various types of business districts throughout the city is the result of economic forces, the pattern of importance of location and uses within a district is also the result of the same economic forces.

A knowledge of what similar businesses are doing in other near-by locations enables the appraiser to judge the relative advantages and disadvantages of such locations and of the property to be appraised. However, in making this analysis, account must be taken of the inherent capacity of some retail types to pay higher rental than others. Richard U. Ratcliff, Assistant Professor of Real Estate Management at the University of Michigan, states in a recent monograph:[3]

> "Certain of the retail types appear to possess an inherent capacity to pay higher rents than other types. While such a hierarchy undoubtedly exists, previous discussions of it have failed to emphasize the true nature of the differential exploitive abilities which it reflects. Correctly defined, the hierarchy is not one of retail uses alone, but of retail uses *on appropriate sites*. Thus, while in fact department stores pay higher rents than grocery stores, this situation obtains only when de-

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[3] Richard U. Ratcliff, *The Problem of Retail Site Selection*, Michigan Business Studies, Vol. IX, No. 1 (Ann Arbor, University of Michigan, 1939).

partment stores are properly located, for were a department store situated in a neighborhood retail cluster it could pay no rent at all. It should be further stated that for each site there exists a hierarchy of uses based on their rent-paying ability on that site, and that there is a hierarchy of sites based on differential productivities under the appropriate uses."

For this reason, the most intensive portion of primary business districts will be occupied by certain types of businesses, whereas other types will be found to be located in the peripheral area. Certain types of businesses, because of the frequency of their occurrence together in the same block, will be found on examination to have an affinity for each other.

Business fluctuates with economic conditions, and at least five years' past business volume should be studied in arriving at a conclusion of rental value. However, in using such information as a basis of rental estimates, the appraiser must be sure that the existing occupancy represents the best use of the site as the property value does not attain its maximum value unless occupied in such a way as to develop its greatest economic use.

The data given below are from a typical business property in the primary class located in one of the primary outlying business districts of Chicago—the Harlem Avenue and Lake Street business district located in Oak Park, a western suburb of Chicago.

The gross volume of business reported for the year ending December 31, 1938, shows the following:

Store No.	Gross Volume of Business 1938	RENTAL PAID—1938 Minimum Rental	Excess	Total
1	$360,310	$24,000	$1,221	$25,221
2	155,230	12,000		12,000
4	140,120	9,000	808	9,808
		$45,000	$2,029	$47,029
				8,000
				$55,029

With the rental information before him the appraiser proceeds, exactly as he did in the case of the neighborhood property, to analyze the adequacy of the occupancy and the present rentals, their conformance with the level in the locality, and the importance of the location of the property under consideration as compared with other locations in the area.

The location of this example is one of the best in the district's 100 per cent block, which is equally good on both sides of the street. The present tenancy consists of three strong chain-store tenants with a long record of successful operations in Chicago. Independent merchants in this block have not met with the full measure of success enjoyed by the well-known chains, with the result that those properties with strong chain stores are able to justify a better rental than properties rented to some of the independent merchants.

STORE RENTALS AND LEASES[4]
(as of May 1, 1939)
One-Story and Basement, Brick Store Building
Located at 0000 West Lake Street, Oak Park, Illinois

Store No.	Business	Frontage (Feet)	Area (Square Feet)	Period of Lease	Minimum Rental	Rental Percentage of Volume
1	Five-and-ten-cent store	60	13,000	Oct., 1936—20 yrs.	$24,000	7%
2	Chain shoe store	25	3,500	May, 1937—10 yrs.	$12,000	7%—8%
3	Vacant	20	2,500	(ask)	$ 8,000	
4	Women's wear store	20	4,000	Oct., 1936—10 yrs.	$ 9,000	7%

This business center is one of the most spectacular primary outlying business districts developed in the last ten years by the trend toward decentralization. It serves a part of the great west side of Chicago and affects adversely old, established business sections as far east as the Crawford-Madison district (several miles away). It serves Oak Park, River Forest, and the western area of Chicago.

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[4] Although some slight adjustment has been made in these figures so that they cannot be identified with the actual property from which they were taken, they are nevertheless undistorted in relationship to each other and are representative of an actual property.

Large Chicago department stores and chain-store organizations were quick to recognize the potentialities of this area so near to a large market, and the area has grown by leaps and bounds in the past five years. The result is that at the present time this business center includes branches of four large Chicago Loop department stores and many chain stores and merchants found in the Loop district.

Harlem Avenue is the Oak Park-River Forest boundary. Lake Street west of Harlem Avenue is a one-sided street, the land on the north side of the street being a large public park several blocks square.

In 1937, business development jumped across Harlem Avenue to River Forest. The first building was Wieboldt's new department store on the southwest corner, followed by a tail-end satellite development of one-story stores for the remainder of the block. Wieboldt's store and, to an even greater extent, these tail-end stores are offsetting the drawback of being out of the 100 per cent block by offering adequate parking facilities adjacent to or in the rear of their stores. There does not, however, seem much likelihood of the Lake Street development successfully extending much farther to the west.

An analysis of the present rental level of the stores in the afore-mentioned example shows that two stores earned rentals slightly above their minimum rental, one store almost reached the minimum rental, and one store is vacant. This is the only vacant store in the 100 per cent block and has been held for the purpose of finding a strong tenant. The minimum rental charged on these stores is compatible with other rentals prevailing on other properties in the block. The appraiser assumes that the vacant store will be rented within a reasonable time at approximately the rental asked. In analyzing the 1937 volume of sales transactions, the appraiser finds them to be higher than the 1938 volume. Based upon his study of the district, he makes his estimate of gross income upon the basis of the present rental now being paid (and earned) by responsible tenants plus the rental for the vacant store, which he assumes will be rented to an equally strong tenant very shortly. He assumes that this 1938 rental level will obtain for one year and that improved business and operation of the percentage clauses in the leases will tend to increase these rentals 5 per cent each during the second, third, and fourth years, at which point they will remain stable. He assumes that an informed buyer would be justified in estimating the probable future rental upon this basis. The estimate, therefore, would be as follows:

Store No.	Rental Paid 1938	Estimated Rental			
		1939	1940	1941	1942
1	$25,221	$25,221			
2	12,000	12,000			
3	(Vacant —ask $8,000)	2,000 (¼ yr.)			
4	9,808	9,808			
	$47,029	$49,029	$57,750	$60,000	$62,750

It is possible that substantial improvement in business conditions will increase the rentals to the owner (through operation of the percentage clause) more than the increases estimated. However, in the light of informed opinion as it stands today, an assumption of greater rental increases for the future than is shown here becomes increasingly speculative as the appraiser moves his estimate upward from present rentals.

GROSS INCOME OF CENTRAL-BUSINESS-DISTRICT STORES

The five cases for which figures are here given represent actual present occupancies on the main retail shopping street in the central business district of a large midwestern metropolis. They indicate differing conditions confronting appraisers who must estimate future store income on central-business-district property. In each case the figures used have been adjusted by a uniform percentage to prevent identification, but at the same time the relationship of each volume in the various years and its relation to rental and size of the premises have been preserved. For the same reason, the kind of business is not stated, although the proper percentage that this business can afford to pay as store rental is given.

The older central business district of a city develops certain problems not found in the newly developed outlying district. As retail productivity is affected by location, site competition takes place among merchants for the more intensive locations. This competition is more or less keen, depending on business conditions. In the period from 1925 to 1929 competition for locations became so keen that sales over past years were lost sight of and new leases were based upon estimates of future conditions upon a continuing-expansion basis. Instead of sales increasing, the depression brought decreased sales.

Many such tenants, including some who were considered to be entirely responsible, failed under the tremendous financial pressure of this situation. A few proved strong enough to survive, mostly through their ability to readjust a good many such leases which they had made. In a few cases where they could not readjust, they are still being forced to pay rentals out of proportion to the volume of business done and are paying this rental out of operations of their other stores. In many cases these leases have involved long litigation which has been expensive to both lessor and lessee. The lessee has made frantic attempts to be relieved of the pressing burden of a rental many times the amount that can be earned at the location. Case No. 1 is an actual example of such a situation. An analysis of the prevailing current rental levels would indicate that had this lease been negotiated subsequent to 1933, it probably would have provided for a minimum annual rental of $20,000 to $25,000 instead of the $70,000 being paid under the 1927 lease.

CASE NO. 1

Frontage: 25 feet (irregular).

Depth: 120 feet.

Area: 3,500 square feet; basement additional.

Term of lease: 25 years from May 1, 1927.

Rental: $70,000 per year. Owner furnishes heat, pays taxes and all expenses. Tenant pays own interior maintenance and repairs.

	1934	1935	1936	1937	1938
Gross volume of sales	$245,000	$240,000	$245,000	$250,000	$190,000
Actual rent received	$70,000	$70,000	$70,000	$70,000	$70,000
Relation of rent received to sales	29%	29%	29%	28%	37%
Per cent business can afford to pay	6%	6%	6%	6%	6%
Justified rental value based upon value of land	$14,700	$14,400	$14,700	$15,000	$11,400
Excess rental paid	$55,300	$55,600	$55,300	$55,000	$58,600

In estimating the future gross income of a store where such a situation exists, the appraiser is forced to include something of value that is not inherent in the real estate nor secured by it but is inherent in the financial strength and responsibility of the lessee. In this case the lessor has only the same security of income that he would have if he were holding the lessee's note, without any real estate security; and he has a tenant who may be inclined to use every possible opportunity to be relieved of this obligation. This, of course, increases both the insecurity of the income and the management burden. Expensive lawsuits must frequently be contested before the tenant can be forced to pay.

Therefore, the appraiser must estimate the probable fair future rental that could be obtained from a tenancy not obligated under such an old lease in order to judge the extent to which the rental is excessive. He must then determine the financial responsibility of the tenant, how completely the tenant is legally bound by the lease, and the probable added cost of collection. If a higher rental is collectible, even if excessive, it obviously must be taken into account in the income estimate.

The minimum rental is generally provided in the percentage lease to cover the taxes and other expenses of the owner. Where only a minimum is provided, the owner may find that he has a tenant who cannot exploit the full possibilities of the location. Case No. 2 is an example of an actual central-business-district property where an old, established business moved out and a new tenant took possession under a straight percentage lease.

CASE NO. 2

Frontage: 30 feet.
Depth: 150 feet.
Area: 4,500 square feet; additional space: entire 5-story building, of which first and second floors are used for sales, remainder for storage.
Term of lease: 8 years from May 1, 1938. Previous tenant was in same line of business but handled more expensive merchandise.
Rental: 8% of sales volume; no minimum rental. Recapture clause in lease whereby lessor may at his option cancel lease if rental reaches $22,000 per annum in 3 years. Owner furnishes heat and pays taxes and expenses. Tenant pays own interior maintenance and repairs.

	1934	1935	1936	1937	1938 (8 mos.)
Gross volume of sales	$350,000	$339,000	$350,000	$400,000	$120,000
Actual rent received	$28,000	$28,000	$28,000	$32,000*	$9,600**
Relation of rent received to sales	8%	8.3%	8%	8%	8%

*Paid excess under percentage clause.
**Actual 1938 rental collected includes that paid for part of year by old tenant and part of year by new tenant, but 1938 figures shown here are the figures for new tenant for the last 8 months of the year.

From the information about the past volume of business done in these premises and about the rental paid, it does not seem that this new tenancy is a proper use for the premises. In estimating the future income on this store, the appraiser must estimate the fair future rental value of the property, based upon an analysis of what similar surrounding stores are doing in volume and paying in rental. If, after such analysis, it still appears that the present store is not utilizing the potential possibilities of the location, the appraiser must estimate the fair future rental for the premises.

Since the property will continue with the present occupancy until May 1, 1941, the appraiser must estimate the probable rental that will be produced by the present tenancy to that time. He must inform himself as to the reason for the very low sales volume done on the premises and the chances of an increase to a normal figure for the location. In any event, he must assume that, if the present tenant does not reach the fair rental level by May 1, 1941, the owner will exercise his privilege (under the recapture clause) to cancel the lease and find a new tenant who can pay the fair rental.

Where the volume of past business seems to substantiate the rental paid for the premises and where this has further confirmation in other rentals of properties with equal advantage of location, the past rental forms a very good basis for the appraiser's estimate of future rental conditions. Case No. 3 is an example of such a situation.

CASE NO. 3

Frontage: 30 feet on main street, 100 feet on side street.
Depth: 100 feet.
Area: 3,000 square feet, plus selling basement.
Term of lease: 10 years from May 1, 1934.
Rental: 8½% of sales volume; $30,000 per annum minimum guarantee. Owner furnishes heat and pays all building expenses. Tenant pays for interior store maintenance and repairs.

	1934	1935	1936	1937	1938
Gross volume of sales	$315,000	$318,000	$406,000	$402,000	$350,000
Actual rent received	$30,000	$30,000	$32,480	$32,160	$30,000
Relation of rent received to sales	9.5%	9.4%	8%	8%	8.5%

In making an analysis of current rentals paid on other properties, the appraiser should be careful to get all facts surrounding the lease and should not jump at conclusions. Case No. 4 is an example of leases under which, in order to determine the rental cost of the premises to the tenant, additional amounts must be added to the actual rental paid the owner. In this case the tenant rebuilt the building at an expense of $35,000. Obviously, had the owner made this added investment in the structure, he would have been compelled to charge a higher rental to get a return on the additional investment. Therefore, the true rental cost of the premises can be determined only by adding to the rental paid by the tenant an interest return and a depreciation allowance on the tenant's building investment.

CASE NO. 4

Frontage: 25 feet.
Depth: 100 feet.
Area: 2,500 square feet, plus old shell of building.
Term of lease: 10 years from May 1, 1935.
Rental: 8% of sales volume; minimum guarantee $30,000 per year. Entire premises remodeled into a 5-story building by tenant at cost of $35,000, but owner pays all taxes and insurance.

	1934	1935	1936	1937	1938
Gross volume of sales				$280,000	$260,000
Actual rent received				$30,000	$30,000
Tenant's depreciation and return at 8%				$2,800	$2,800
Rental of store only				$32,800	$32,800
Relation of rent received to sales				11.7%	12.6%

In some cases, the tenant contracts to pay a certain rental to the landlord and, in addition, to pay the taxes. Case No. 5 is an example of this type.

CASE NO. 5

Frontage: 50 feet.
Depth: 120 feet.
Area: 6,000 square feet; additional space: 5-story building used for sales, service, and storage.
Term of lease: 5 years from May 1, 1939 (a new lease made at the expiration of a former lease).
Rental: 6% of sales volume; minimum guarantee $50,000 per year plus taxes. Tenant to pay taxes and all operating expenses.

	1934	1935	1936	1937	1938
Gross sales volume	$650,000	$700,000	$775,000	$800,000	$725,000
Actual rent received	$40,000	$40,000	$40,000	$40,000	$40,000
Adjustment for additional space	$23,000	$23,000	$26,000	$24,000	$25,000
Insurance and operating expenses	$2,000	$2,000	$2,000	$2,000	$2,000
Tenant's rental cost	$65,000	$65,000	$68,000	$66,000	$67,000
Relation of rent received to sales	10%	9.3%	8.7%	8.2%	9.2%

Examination of the fluctuation of the sales volume in the five cases cited shows the upward trend, with improving business conditions, of 1936-37 and the subsequent decline in sales for 1938, as a result of business recession. The extent to which future sales volume will be affected by worse or improved conditions will accordingly affect the future rental of the stores in the district. This obviously increases the difficulty of the appraiser's task of estimating the future rentals that the stores will produce. It also brings out one of the disadvantages of the percentage lease, in that mortgage lenders recognize a hazard in this situation of a fluctuation in income and rentals and therefore hesitate to reflect more than minimum rentals in their appraisals for financing.

In the final analysis, the accuracy of a real estate valuation must stand or fall with the accuracy of the income estimate. It is the justified value that is ultimately sought, and it must be kept in mind that an informed purchaser will be guided by his opinion of the income that the property will produce. His opinion will be extremely conservative, even pessimistic, in times of depression; while in boom periods it is likely to be extremely optimistic. The present earnings of property, of course, are of great weight in any estimate of future earnings because they are a tangible, existing fact and will influence the informed purchaser in considering the future trend of rentals.

THE VALUATION OF HOSPITALS

Lottie L. Crawford, M.A.I., and Victor R. Lundy, M.A.I.

OPPORTUNITIES for the appraisal of hospitals are comparatively rare, and there is little to be found in appraisal literature dealing with this subject, the extent of the discourse on hospitals being that they are service properties and as such are to be appraised upon a cost less depreciation basis. With the scope of the problem thus defined, the job of appraising a hospital appears on first thought to be one having to do almost entirely with brick and mortar. However, a casual consideration soon reveals that in such an appraisal many interesting and sometimes intricate problems are involved.

Hospitals, it appears, while generally classified as service properties, have in numerous cases many of the attributes of investment properties. The plant and equipment, the personnel, the receipts and disbursements, the problems of management in a hospital are often more intricate than those of large and important commercial enterprises; and the necessity for most of them to earn a return commensurate with the capital investment which they represent is no less than it is in the case of hotels, apartments, and similar enterprises which have, as do hospitals, space and service for sale, and the investment nature of which is recognized.

Hospitals may be grouped into three categories, based upon the types of control under which they are administered, as follows: (1) *governmental,* including Federal, state, county, and city hospitals; (2) *nonprofit* associations, including independent associations, churches, and fraternal orders; and (3) *proprietary,* including individuals or partnerships, corporations, and industrial enterprises.

The nature of the various governmental hospitals is familiar to all of us and deserves no particular comment here. Capital invested in such properties is largely that raised by taxation.

The nonprofit-association hospitals include all those operated in such a manner that the gains or losses of the hospital do not accrue to the personal account of the investors who supply the capital or control the policies. The nonprofit designation does not imply that such institutions are free from the pecuniary necessity of showing a return on invested capital, much of which is frequently represented by mortgage bonds or other forms of indebtedness which require the usual servicing.

Proprietary hospitals include all those organized upon a business basis with a view to earning a profit for the individuals or corporations supplying the capital and controlling the financial policies.

Except in the states of California, New Mexico, and Wyoming, nonprofit hospitals are partially or completely exempt from taxation; but in these three states such institutions carry a load along with other real estate in proportion to what is alleged to be their value. In California, which is the field of our endeavor, hospitals are subjected to the same standards of valuation as are other properties of comparable scope and construction, the theory being that the assessor, by the procedure of equalizing valuations upon the basis of quantities of brick and concrete and other materials in a property, is equalizing in fact as required by law. It was for the purpose of analyzing the soundness of this theory that an appraisal of a major nonprofit hospital in a southern California city was undertaken.

AN ACTUAL HOSPITAL APPRAISAL

The hospital appraised consists of two principal buildings of concrete and tile, Class "B" construction, erected between 1924 and 1928, and with a rated capacity of 286 beds and 50 bassinets. In addition, there is a laundry and boilerhouse and a refrigeration plant.

In 1929 a reappraisal of the entire city in which this hospital is located was made, and at that time the cost of replacing these buildings at the then prices was estimated at $1,111,000. By adjusting for changing building costs and applying an annual depreciation factor of 1½ per cent, the assessor had revised this figure downward until at the time of the appraisal his valuation was $655,840.

There was in this case no reason to question the basic cost figures involved nor the manner of adjusting them for changing market conditions; however, the depreciation allowance of 1½ per cent, implying as it does an economic life expectancy of sixty-seven years, seemed entirely inadequate. The justification for this rate, as it finally developed, was not that it is an adequate expression of the rapidity with which a sound fiscal policy would require the recapture of the investment in this property but rather that the rate was applied to all buildings of this type of construction and that, therefore, equality was obtained even though it was based upon a more or less arbitrary and erroneous assumption. As applied to the ordinary run of commercial buildings, subject to the fluctuating interplay of the forces of supply and demand, this theory would, over a period of time, undoubtedly find some support in fact. However, the inclusion of hospitals under such a blanket application of a depreciation factor provoked considerable doubt as to its validity.

PHYSICAL AND ECONOMIC LIFE OF HOSPITALS

Consideration of the functions and the highly specialized type of service which hospitals give reveals that depreciation in all its phases takes a heavy toll. *Physical deterioration,* or that phase of depreciation which has to do with the actual wearing out of the structure, its disintegration and loss of ability to withstand the elements, proceeds in hospitals at a rate comparable with that found in other buildings of similar construction. Isolated instances occur where hospital buildings have actually remained in use for one hundred years or more, and it is said that some of the institutions in Europe at the present time were erected three or four hundred years ago. Those familiar with the quality of service which these institutions make possible report, however, that the fact that they are still in use is of historical interest rather than of scientific value. Structurally, it is apparent that well-constructed buildings, including those devoted to hospital use, if given proper maintenance, will remain standing indefinitely. However, physical wear and tear is only one phase of depreciation and, as applied to hospitals, is not the most important.

Hospitals are apt to suffer in a large degree from *functional obsolescence,* or that phase of depreciation which has to do with the inability of a structure to perform effectively the function for which it was erected. Advances in the science of medicine and hospitalization bring about the necessity for continual change in the methods of caring for the sick. Hospitals which are modern in every detail when built soon become obsolete and inadequate; if they are to endure for a long period of time as economic units, large sums of new capital must be invested in them for purposes of modernization and rehabilitation.

Dr. C. Rufus Rorem in his illuminating book, *The Public's Investment in Hospitals,* reports the investigation of eighty-five hospital projects which came to his attention, involving a total expenditure of $57,803,000. Of this group only twenty-four, or an expenditure of $15,483,000, represented the foundation of entirely new hospitals. He states: "The improvement, rather than expansion, of facilities has been a characteristic feature of recent hospital construction." Such a situation can have only one result, and that is loss of value at a rapid rate in existing hospital structures.

Further confirmation of this conclusion was found in the results of a survey, made by the authors as a part of the afore-mentioned hospital appraisal, of 1,000 hospitals in the United States accredited by the American Medical Association. Questionnaires were sent to all nonprofit and proprietary institutions in California of 50 or more beds and in other states of 100 beds and over. Only those institutions which might be considered as operating upon a competitive basis were included. Information was returned on a total of 384 of these hospitals.

Results of this survey when tabulated showed that in the twenty-years-and-under age group not only had a number of hospitals been demolished, but that 20 per cent of them had required new capital expenditures for modernization. In the twenty-to-thirty-year age group, 72 per cent were reported as either modernized or demolished. And considering all reporting hospitals, it was indicated that before reaching the age of forty years, 60 per cent of them had been demolished or had undergone one or more extensive modernization programs.

Results of this limited survey are, of

DEMOLITION AND MODERNIZATION OF HOSPITALS

	Years of Actual Age	1 to 20	21 to 30	31 to 40	41 to 50	51 and Over	Total All Ages
Age at which First Modernized	1 to 20	25	54	24	10	4	117
	21 to 30		6	25	11	7	49
	31 to 40			7	10	6	23
	41 to 50				3	2	5
	51 and over					4	4
	Total Modernized	25	60	56	34	23	198
	Number Demolished	3	7	20	9	7	46
	Modernization Not Indicated	98	25	2	5	10	140
	Number in Group	126	92	78	48	40	384
	Per cent of Total	33	24	20	13	10	100

The above figures are the result of a questionnaire sent to 1,000 hospitals throughout the United States accredited by the American Medical Association and excluding all city, county, state, and Federal hospitals or those of fraternal or industrial organizations. Only those were considered for which the making of a profit might be an important consideration. Included were such hospitals in California of 50 or more beds and in other states of 100 or more. Information was returned on a total of 384 hospitals.

course, not conclusive, but they do appear to support the conclusion that the probability of any hospital enjoying, without the addition of large amounts of new capital, an economic life of sixty-seven years is extremely remote and that a depreciation factor of 3 per cent, as advocated by some hospital authorities, is much more realistic than 1½ per cent.

From the information on the 384 hospitals considered, the following data were developed: Thirty-three per cent, or 126, were less than twenty years old; 57 per cent, or 218, were less than thirty years old; 77 per cent, or 296, were less than forty years old; 90 per cent, or 344, were less than fifty years old; only 10 per cent were over fifty years old. Three were demolished before they were twenty years old; 10 were demolished before they were thirty years old; 30 were demolished before they were forty years old; 39 were demolished before they were fifty years old; 7 were demolished after they were fifty years old; a total of 46 hospitals were demolished. Twenty-two per cent of the hospitals under twenty years old were either remodeled or demolished; 72 per cent of those twenty-one to thirty years were either remodeled or demolished; 97 per cent of those thirty-one to forty years were either remodeled or demolished; 89 per cent of those forty-one to fifty years were either remodeled or demolished; 75 per cent of those fifty years or older were either remodeled or demolished.

ECONOMIC FACTORS INVOLVED

Economic obsolescence, or that phase of depreciation which has to do with the loss of value due to adverse economic factors not inherent in the property but rather environing it, has special effect as applied to hospitals. In a consideration of standard properties, well-built and properly designed, we find that their value tends to adjust to the cost of producing them and that loss of value due to physical deterioration and functional obsolescence accrues only as the result of the passage of time and is more or less accurately a function of time. Economic obsolescence, however, does not involve a time element, and, as is especially true with regard to hospitals, many properties at the time of completion, although structurally and functionally adequate, are worth less than their cost due to adverse economic factors involved.

A hospital is subject to peculiar economic hazards. It is a civic and social institution which, unless it co-operates freely in promoting community well-being, is thought of as not performing the task for which it was intended. The result of this situation is that it is exceedingly difficult to operate a hospital upon a strictly commercial basis, and, to the extent that its efforts are devoted to charitable activity and free service, it becomes uneconomic and suffers loss of value accordingly inasmuch as it grows impossible for it to earn a legitimate return on the capital investment which it represents.

The pressure of this public demand is such that a tendency is reported in recent years for hospitals, originally organized as proprietary business ventures, to reorganize as independent, nonprofit associations in order that the original entrepreneurs may be relieved from the social pressure which tends to make their enterprise economically unsound.

In all states, with the exception of those mentioned, this situation is recognized, and an effort to compensate for it is made by the elimination of taxes wholly or in part. Where no such tax concession is made, there appears to be logic to the contention that, in so far as charitable activity results in a loss of capital value, the inequality which thus arises should be adjusted by a proportionate reduction in valuation for tax purposes.

Suppose, however, that we take the point of view that charity and free service are not legitimate functions of a hospital and that we convince not only ourselves of this point but also the hospitals, with the result that they resist the public pressure and refuse the charitable demands made upon them. In the particular case studied, and there are probably many others where comparable conditions prevail, this results in a strange and untenable situation.

When an owner shows that a portion of his building is uneconomical and desires to close it against use, it is the practice of the assessor in the particular city involved to give a large reduction in tax valuation for as long as that nonuse continues. The paradoxical result would be, then, that by removing a portion of its plant from charitable use and allowing it to lie idle, the hospital would be relieved of the large tax which it must pay as long as that portion of the building is devoted to public charitable use.

INCOME AND OPERATING FIGURES

Consideration of some typical figures involved will illustrate the application of the concepts already discussed.

INCOME AND EXPENSE STATEMENT

Annual gross income expectancy....		$494,655.00
Expense, paying guests	$382,895.00	
Expense, free service	24,710.00	
Net cost, nurses' training................	27,490.00	
Recapture of capital investment in furniture and equipment in twenty years—.05 x $50,000........	2,500.00	
Interest on investment in furniture and equipment—.08 x $50,000....................................	4,000.00	
Tax on land and equipment............	880.00	
Interest on land—.07 x $7,000........	490.00	
Reserve for replacements.................	2,485.00	
		$445,450.00
Net before return of capital in and interest and taxes on improvements		$ 49,205.00
Capitalized at 14.5%		
Tax value indicated for improvements		$339,345.00

The income and operating figures presented above were developed from detailed hospital accounts for several years past and grouped, for the sake of convenience in referring to the records which were set up, under these broad headings. They represent, upon the basis of past performance, what appears to be a reasonable expectancy. Because of their unusual nature, certain of these items deserve some explanatory comment. It is inferred that the reader will accept this as a properly reconstructed income statement.

Nurses' training is generally considered to be a legitimate and necessary function of a large modern hospital. There is some thought that this should be handled by the state as a part of its program of public education, but to date the maintenance of a competent supply of nursing talent has depended upon the training schools conducted by individual institutions. The cost of giving such training, it is generally felt, is justified on economic as well as social grounds.

The proper procedure for recapturing the capital investment in furniture and equipment is one over which there often is, and might be in this particular case, considerable discussion. The correct rate of depreciation cannot be stated in one amount. Furniture tends to be unsuitable for hospital use at the end of approximately ten years, although in some instances it may remain in service for a much longer period. In general, specialized equipment for medical and surgical care may be expected to become obsolete after approximately five years of use, with some of the particular types of equipment having a useful life of only two or three years if the hospital expects to keep step with the advance in medical science.

It is assumed in this particular problem that furniture and equipment are in an acceptable condition, that a fairly regular expenditure has been made annually for replacements and repairs, and that it is logical to conclude that a continuation of these expenditures, which were hidden in the hospital statement under various departmental expenses, over the remaining estimated economic life of the property would maintain the furniture and equipment in approximately its present condition without any major capital investment in any one year. Based upon this assumption, the return of capital or depreciation could be estimated upon the basis of twenty years, as indicated, $50,000 being the value assigned to this portion of the investment in its existing condition.

Capital and tax charges as set out require no comment except that the question as to a proper rate to reflect the many unusual hazards involved should be the subject of serious consideration. A reserve for structural replacements would, of course, find the same application in hospital buildings as in others of similar construction.

Perusal of the expense statement indicates that the value reflected to the improvements will be from the residue of income available after other capital charges are made. This appears to be the logical approach in a case of this kind where depreciation is a factor of such uncertain quantity.

It will be noted that the net obtained is before taxes on the improvements as well as before interest charges on the capital invested in improvements and provision for return of that capital. Obviously, if it is claimed that the existing tax appraisal has been erroneously made and that the present tax is, therefore, in error, the calculation of a proper tax must wait upon an acceptable value estimate. We do have, however, a tax rate which states taxes as a percentage of value. If this tax rate is applied in the capitalization of the net income, the proper allowance for taxes is made without actually including taxes as a deduction from income in the statement. In this particular case the tax rate which applies is 2.63 per cent on full valuation.

A reasonable return to capital invested in these improvements is taken as 7 per cent, this being a rate indicated upon the basis of market requirements from other properties of comparable hazard.

Provision for return of capital investment in the improvements over the estimated remaining economic life of twenty years is made upon a straight-line basis of 5 per cent per year. A depreciation charge of this proportion appears to be unreasonably large at first glance. However, it becomes apparent that 5 per cent, as here used, is applied to the remaining value of the improvements and amounts to approximately the same thing as charging 3 per cent against original value.

It is quite probable that at the end of twenty years this hospital will still be in use and that its economic life, due to extensive rehabilitation, may extend well beyond the number of years assigned to it. This probability might logically have been taken into account by providing for amortization of all capital over a longer period of, say, thirty or forty years and, in addition, setting up an annual reserve to provide not only for the usual replacements but also for rehabilitation and modernization. In an appraisal for most purposes this procedure might be preferred. However, in an appraisal to establish a basis for taxation, the procedure as followed was indicated.

Assessors do not adjust their appraisals to take account of a new roof, painting, and various replacements in the plumbing equipment, heating system, etc. A property with a new roof, fresh paint inside and out, and in first-class condition in every regard is worth no more to the assessor than the same property in need of paint and repairs. Programs of modernization, however, are accounted for by the assessor in a readjustment of value but not by any change in the depreciation factor applied to the property. It is necessary, therefore, in order to follow a procedure comparable to that used by the assessor, to apply a rate which assumes no new capital expenditure in modernization.

Obviously, depreciation in a property of this type, as it accrues, will be reflected in a declining net income imputable to the improvements. It is in recognition of this fact that a straight-line depreciation factor is used, the implication being, of course, that the net will decline in an annual amount which is equal to interest on returned capital. The fact that gross income may remain stable or even increase does not necessarily invalidate this assumption, for such a result, it is felt, could be obtained only because of additional capital expenditures or increased operating costs or changing value of the dollar.

Taking into account these three factors just discussed we have a combination rate to be applied to net income made up as follows:

Tax rate	2.63%
Return on investment	7.00%
Return of investment	5.00%
Total combined rate (say)	14.50%

ACCRUED DEPRECIATION

Application of this rate to net income before taxes, interest, and depreciation results in a figure which is the indicated tax value of the improvements. Tax value is supposed to be market value. However, there is one situation in which these two values clearly cannot coincide, and that is found where a substantial allowance for accrued maintenance and replacements must be made, as in the case under consideration. The market values of two properties, one completely renovated and one with considerable accrued maintenance, are considerably different and can be adjusted only by an allowance of a sufficient amount to bring the run-down property up to standard condition, plus, in many cases, a profit for doing so.

In the hospital under consideration the expenditure of a sizable amount was indicated in order to bring the improvements to a condition assumed in the estimate for accrued depreciation, and the property had an indicated market value which was less by this amount than the tax valuation found. This expenditure was not one which would be reflected in an increased net income, but failure to make it within a reasonable period of time would most assuredly result in a loss of income, as will be evident from a consideration of the items involved.

NECESSARY REPLACEMENTS AND REPAIRS

Replace boilers	$ 9,000.00
Paint exterior	7,000.00
Install new elevator	9,000.00
Replace laundry equipment	7,500.00
Put on new roof	1,200.00
Renew plumbing	8,300.00
Estimated necessary expenditures	$42,000.00

It is to provide for expenditures such as these that in the statement an annual charge is set up under "Reserve for replacements." No income can be counted as net income until account has been taken of this reserve, even though in many years no such expenditures will be made. This required expenditure does not, therefore, represent new capital investment at this time but rather an expenditure of funds accounted for by an annual deduction, as shown in the statement of income and expense.

Adjustment to market value upon the basis of our present figures gives us the following:

Tax value indicated for improvements	$339,345
Estimated necessary expenditures	42,000
Indicated market value	$297,345

COMPARISON OF VALUATIONS

We have at this point a basis for the following value comparisons:

Tax valuation by assessor	$655,840
Tax valuation indicated by earnings	339,345
Difference between valuations	$316,495

What appears offhand to be an irreconcilable divergence lends itself to a very logical and interesting explanation. As previously stated, the assessor's valuation is based upon the use of a depreciation factor of 1½ per cent. However, the evidence indicates that this is an entirely inadequate rate as applied to hospitals and that a rate of 3 per cent, implying an economic life of thirty-three years, could be more logically applied. Revising the assessor's figure to take account of this rate, we have:

Tax valuation on 3% depreciation basis	$510,560
Tax valuation indicated by earnings	339,345
Difference between valuations representing economic obsolescence	$171,215

Assuming our calculations to this point to be sound, the discrepancy shown above represents economic obsolescence or loss of value due to failure of the property to show an adequate earning because of adverse economic factors. Referring to the statement of income and expense we find an item, "Expense, free service, $24,710." This represents an actual deduction from income because of the charitable activities of the hospital, and we are not surprised to find that when the rate of 14.5 per cent, as already explained, is applied to this figure, a loss of capital value of $170,400 is indicated. The difference between this figure and the one obtained above is so slight as to indicate that practicallly all of the economic obsolescence involved is due to the expenditure for free service. In other words, it is indicated that, if the item of free service could be eliminated from the statement, the property would show a net earning commensurate with the cost of replacing it.

CONCLUSION

The appraisal of a hospital for a purpose other than that of taxation would, of course, call for a different handling of some of the problems involved, although many of the same fundamental considerations would apply. It appears that a well-conceived and properly operated nonprofit or proprietary hospital has the possibility of earning an income commensurate with the cost of producing it. A large proportion of the charges of such institutions are made upon a strictly business basis, which, if applied to all of their operations, would result in a net earning suitable to the investment. However, the requirement for charitable activity and free service prevents the realization of this potentiality.

In so far as failure to earn on cost is the result of this charitable service, it might be held with apparent justice that a hospital is worth cost and that it is only when failure to earn on cost is in an amount greater than the contribution in charitable activity that a hospital can be said to suffer excess depreciation. In other words, if it is assumed that all hospital guests are paying guests, taking the usual account of losses due to bad debts, then we have a measure upon this theoretical basis as to whether or not the hospital earnings reflect a value commensurate with its cost. We shall find under such an assumption that cost and value as reflected by income tend to correspond just as they do in all investment properties.

It would appear from this point of view, even though summation is accepted as the proper approach to hospital valuation, that a careful analysis of the income and expense statement can be of considerable importance as a check on the proper allowance for accrued depreciation and in bringing to light certain phases of depreciation which might otherwise be overlooked.

THE FOLKLORE OF VALUATION

ROBERT H. ARMSTRONG, M.A.I.

FOLKLORE is a term coined in the year 1846 as a designation for the traditional learning of the uncultured classes of civilized nations. Perhaps it is a far cry from the state of being uncultured to that of being an appraiser; but there is no doubt that we have been and are affected to no slight degree by folklore in the science of valuation.

More particularly, folklore pertains to the traditions, customs, and beliefs of people. Appraisers, in some ways, form a unique group, and, just as has any race, so do we in our field have our special traditions, beliefs, and customs—in short, our own folklore. Few appraisers, however, are willing to discuss this subject. The customs and traditions of the science of valuation are treated as if they were skeletons in the closet, with the less said about them the better. Therefore, a bit of investigation into some of our own very special folklore may be worth while.

What is our heritage? In what manner have we been trained to think and reason? And why is it that we form our mental concepts in the way that we do? It would be pleasant to believe that education has set our minds free, but such is not the case. With no disrespect, attention is called to that dictum of the Church, with which psychologists are in total agreement, "Give me a child till he is ten, and you can have him the rest of his life." I am sure the implications can be understood without further explanation.

We are all the children of two factors—heredity and environment. That being the case, it is natural that we should take for granted those things to which we have grown accustomed. It follows also that those things to which we are not accustomed and which differ from the past are oftentimes regarded as abnormal.

All of us, seeking introspectively the solution of the problems of our calling, depend upon certain patterns of human behavior. Because we have learned that human beings usually react in the same way when confronted with certain situations, we are wont to depend upon the repetition of the human behavioristic pattern when we are called upon to give our judgment and opinions.

OUR APPRAISAL HERITAGE

To say that our economic system has changed terrifically during the past decade seems superfluous. However, have we as human beings changed very much? What appears to be our basic trouble is that human beings cannot change and cannot adapt themselves to new economic conditions as rapidly as those conditions come upon us. We are prisoners, then, of folklore. Too often we have accepted our heritage from the past without question and without regard as to whether that heritage would prove an influence for good or bad. Therefore, at this point it is in order to review briefly the history and the use of our three primary concepts of valuation: (1) supply and demand (otherwise known as market data—sales, rents, offers to buy, offers to sell), (2) cost, and (3) income capitalization.

Almost two thousand years ago Publius Syrus, who was born in the year 42 B. C., stated one of the first applied rules of value in the words, "Everything is worth what the purchaser will pay for it." Malthus restated the case 130 years ago, and the majority of appraisers have come to depend to a greater or lesser degree upon market sales in establishing the worth of property. Therefore, our heralded comparison approach in valuation is nothing new; it is so old that it may well be called a tradition.

Another method of valuation upon which many depend is based upon the fact that cost determines value. That, too, is nothing new for in the year 301 A. D. Diocletian promulgated an edict which attempted to fix a just price based upon the usual cost of production.

During the Middle Ages the heart of economic doctrines of the times was contained in the words *"justum pretium,"* or a just price. This just price depended upon what was considered a true, absolute value, this being determined by the estimated cost of production — which, it should be noted, included labor. During the Middle Ages market values were regarded as unnatural, and to sell anything for more or less than its cost was usually thought to be unmoral. This line of reasoning was formulated by Thomas Aquinas and Albertus Magnus in the beginning of the thirteenth century. So, after seven centuries, we probably can regard our "cost theory" as being a custom or tradition.

These two methods or theories of value have been the subject of much thought and argument for hundreds of years. Nevertheless, up to the time we began to use capitalization, cost and supply and demand were the main props upon which valuation depended. To that, of course, must be added that "sixth sense" which appraisers also used, about which more will be said hereinafter.

Just when capitalization began to be used for purposes of valuation is difficult to say; certainly it was less than fifty years ago. In fact, it did not come into general use in real estate until a decade or so ago. But what folklore — modern folklore—has surrounded this newcomer! This new baby in the family has taken all the attention away from its brothers—"Cost" and "Market."

Heredity and the way we have accustomed ourselves to think have already been mentioned. Because of its heredity, our new brain child, "Capitalization," has some very discernible family characteristics; in fact, her resemblance to her brother, "Supply and Demand" (alias "Comparative Market Sales"), is most remarkable.

What are these resemblances? A few may be mentioned here, but only a few. When prices are high, rents are usually high; and if an appraiser capitalizes current income, his capitalized value is likely to follow his market. The same thing holds true when rents and prices are low—they usually run together also. It might be said that the projection of income into the future, together with capitalizing future income, overcomes that difficulty. But does it? Human nature being what it is, there seems no particular reason to believe that the appraiser who anticipated the "New Era" in 1929—and who did not?—will not anticipate a new era in rentals when a speculative psychosis or a depression psychosis again takes hold.

Even in an economy which is as controlled as ours is at present, not one businessman, economist, or government official in a thousand or even a million was able to forecast the course of the 1937-38 recession and recovery. Unless an appraiser can project net income with a fair degree of accuracy, his appraisal may fail utterly if he depends upon capitalization alone.

What makes the relationship between the market and capitalization more remarkable is the fact that interest rates are more often than not determined by the market itself. For instance, if purchasers are buying at 6 per cent or 7 per cent, the appraiser is guided by these rates in selecting his rate. However, if he depends upon the public's estimate of interest rates, he most certainly is depending upon the market—and undoubtedly none too accurate a gauge at that.

We have an excellent example of the misconception of both appraiser and the public in the capitalization rates which prevailed when property was bought and sold during the late nineteen-twenties. Call money rose to 15 per cent and 20 per cent, time money earned from 8 per cent to 10 per cent, the commercial-paper rate ran around 4½ per cent to 6 per cent, the grade Baa bond was 8 per cent and 9 per cent, and the Aaa bond yield went as high as 7 per cent and 7½ per cent. Mortgage money averaged 6 per cent.

But at what price did real estate sell? At 6 per cent—sometimes 7 per cent. Common stocks and real estate were out of line with the rest of the world money market, and that is one reason why real estate was inevitably headed for a fall, regardless of whether a depression came or not. If we appraisers cannot do better than to follow the public's and the realty market's concept of a capitalization rate (though it may not necessarily be wrong at all times), we might just as well disregard capitalization for it will amount to no more or less than the market approach to valuation.

It is not our purpose to be critical. We are all well aware of the fact that a statue has never been erected to a critic. But we must go deeper into our theory and practices than we have done heretofore if we are not to be subject to the same criticism in the future as have been our predecessors in the past.

One great similarity of cost, supply and demand, and capitalization is that they are all mechanical-device methods of valuation. Somehow we have been educated to the fact that appraising is not an exact science, but then we turn around and proceed to engulf ourselves in a maze of formulas and figures which would need an Einstein to extricate us—if, indeed, he would know what we were driving at after he did so. Unless the constants are kept as constants, and the variables as variables, all methods of valuation will fail us.

WHAT DO WE APPRAISE?

At this point let us inquire just what it is that we are called upon to appraise when we value a property. Is it bricks and mortar and the land that lies beneath an edifice? Is it these physical characteristics that we appraise? Is it the income that a piece of property returns? Or perhaps the present worth of future benefits to be received?

In answering these questions it might be well to go back to Blackstone who, in his great work, mentioned the fact that the ownership of property consists of "rights." In fact, any ownership is made up of rights; and at times in history these rights of ownership have been many, while at other times they have been few.

The rights of ownership may be likened to a bundle of sticks tied together with a string. A number of sticks in this bundle have been removed, and the unfortunate part of our present position is that we cannot state how many more sticks in that *bundle of rights* are going to be taken away.

Therefore, though we may seem to value bricks and mortar, and land, too, in fact, we never value these things physically. In themselves—and as measured by money—they have no value, no matter what their utility may be. It is *rights*, nothing more and nothing less, which we are called upon to evaluate.

The historical aspect of *rights* in real property need not be considered here. It is true that there have been many restrictions, and many rights have been taken away during the past 250 to 300 years.

However, it seems that whenever a right was taken away in the past, another right was substituted. For instance, we have what are known as zoning restrictions, whereby, to use a simple example, it is illegal to erect a factory in a dwelling neighborhood. While this might prevent some owners from procuring a very high price for their property, it nevertheless protects other owners who would be immeasurably damaged by having adjoining land given over to the use mentioned. Therefore, it might be said that this kind of restriction will actually increase property value for the greatest number of people, or, to say the least, prevent a loss on their part.

Now one essential fact must be stressed at this point: While certain rights have been taken away during the past few centuries, in general they were taken away for the benefit of property owners as a whole.

But the last decade has seen the taking away of the kind of rights from property owners which has tended only to destroy property values, and the present trend indicates that property rights will continue to be removed for many years to come. This has created problems in the business life of the nation, and both property owners and businessmen are finding themselves in the position of children playing the game of "Going to Jerusalem." Every time the music stops there is one less chair to sit down upon. The result is fear and insecurity because none of us knows who will be the next one who cannot find a chair.

In this situation we cannot value property by mechanical methods alone. If we do, we place ourselves in the same position as were those concerning whom the French cynic remarked, "Men go into second marriages, allowing hope to triumph over experience."

HIGHEST AND BEST USE

So far mention has been made of the customs and beliefs which surround the three outstanding methods of valuation. But many of our other theories and practices also come within the realm of folklore, and they most decidedly cannot be judged as was Caesar's wife—above suspicion.

For instance, most appraisers value land according to its highest and best use. But the question must be asked: Why? What may be the best use today may be the worst use tomorrow—witness some of our New York City skyscrapers erected during the "roaring twenties."

However, the greatest weakness of the highest use theory may be illustrated by the following example: Imagine a street—any street—on which business has developed to a high degree. Over a distance of five or ten blocks, one half or two thirds of the buildings are office buildings and large business structures. The remaining one third of the land is improved by various small structures, which are not what would be termed adequate improvements. Perhaps a few of these so-called underimproved lots will support structures of the type already existing on this street; but if all were so improved, the oversupply of office and business space would break the market and cause a decline in values along the whole length of the street in question. Ordinarily each and every one of these lots would be valued for a sum which would justify the highest and best use, but should such an improvement take place on all of the lots, the value of each lot would certainly be less than if only one lot were so utilized.

Another illustration of the fallacy of the highest and best use theory may be gleaned from the sales prices of property in one particular section of New York City in the late nineteen-twenties. Between 59th and

96th Streets on the north and south, Fifth Avenue on the west, and the East River on the east, there were, and still are, something like five or six thousand tenements, each having an age of between forty and sixty years. A great many new apartment buildings, from six to twelve stories in height, had been erected in various parts of this section, but never had the annual rate of construction been more than about thirty buildings; in some years it was far less. Upon the basis of income and risk, each tenement was probably worth somewhere between $20,000 and $30,000 (excluding corners). However, sales of these properties were made at prices ranging from $50,000 to $100,000 each, the higher prices being paid for Avenue frontage. This was at the rate of from $2,000 to $4,000 a front foot. Brokers, owners, and appraisers all predicted great things for this section, and sales were made on the theory of the highest and best use.

Now these 6,000 tenements, each on a plot twenty-five by one hundred feet in size, could make up 1,500 building plots each one hundred by one hundred feet. But if new construction could proceed at its highest rate—up to then thirty buildings a year—it would mean that fifty years would have to elapse before the section could be entirely rebuilt—if, indeed, people could be found in sufficient numbers to live in all of these new buildings. Therefore, the chance that any particular plot would be bought by a builder within a one-year period was one in fifty; and the chance of any one tenement being so used as part of a building plot was only one in two hundred.

Yet so function the minds of men that, when one new apartment was constructed in a certain block, all other land in this block had to be valued according to highest and best use, and not upon income or any other set of factors.

It is not the purpose of this article to present an answer to this problem, but here is a custom or belief which we have inherited which will not stand up in the field of economic reasoning. Yet we talk glibly about highest and best use and, what is worse, use it daily without a thought as to its implications.

MYTHS

Another tenet to which appraisers have long held—and this has been inherited, to a great degree, from the assessors—is that the whole is equal to the sum of its parts, and vice versa. Of course, we have added a few fancy ideas to this—such as 10 per cent for key influence, 20 per cent or 50 per cent for corner influence—all of which have tended to confuse the situation further.

In every city in the country there are lots twenty-five by one hundred feet which are worth only one fourth of the percentage which they bear to a larger plot. If one will travel through the slum sections in our large cities, this will be found to be the case. Then, too, there is the tendency to give plottage additional value when the value of an individual piece may rightly be more than just its percentage of a larger plot of land. Of course, this is not always the case, but the tendency exists to set up rules without the realization that when we come to valuation two plus two does not always and necessarily add up to four.

No doubt mention could be made of many other customs and beliefs which are accepted as gospel, but one or two more examples may well be considered. Most appraisers have at one time or another gone into court, taken the witness stand, and testified in regard to sales in which the principals were supposedly willing buyers and willing sellers. It is asked here, however: Has not the law written implications into the willing-buyer and willing-seller theory which do not actually exist there?

Willingness usually indicates a complete absence of reservations and of compulsions. Due to the fact that in ordinary circumstances the real estate market is limited (real estate does not constitute a liquid asset, such as stock, bonds, or precious stones and articles of that type), most sellers feel that they are not receiving their full price. This unwillingness exists in a greater degree in a static or in a down-trend market than it does in a boom market. Real estate has received speculative profits for so many years in the form of unearned increment that the American people cannot be expected to become accustomed to new conditions brought about by a stabilized population for a good many years to come.

Reasons for selling are many. They include the liquidation of assets, desire to move to a better neighborhood, change of business to a new location, the need of money for business reasons, an increase or decrease in the number of a family, and institutional liquidation. There are many more reasons, and most real estate brokers would agree on the fact that *the willing seller* is indeed a myth.

It is strange how myths become legendary and are finally accepted as fact. Take, for instance, the thought—more or less common at present—that every appraisal shall be as good a number of years hence as it is today. This seems impossible because there are various types of investment. First, there is safe investment, then speculative investment, speculation, and, finally, gambling. If all property is valued from the "safe" viewpoint, it is likely that most appraisals will stand up and prove relatively accurate over a long period of time; but when speculative rates are chosen and speculative property is appraised, appraisals cannot be any safer or surer in the long run than the rate of capitalization which is employed.

For instance, if there are ten pieces of property to be valued and investment is taking place in these properties at a speculative rate of 10 per cent or 12 per cent, the buyer knows that his risk is greater than if he purchases a 4 per cent leasehold. Some of the properties which he purchases may succeed and have a greater value in the future than is indicated by his present consideration. By the same token, some of these properties will be failures, and, in fact, his investment may even be extinguished. The appraiser, in valuing these ten parcels under ordinary circumstances, provided the income and other factors appear the same, may value each and every one of them for the same amount of money. But, because the investments are extremely speculative in their character, the appraiser cannot possibly forecast or measure the present worth of future benefits accurately on each and every parcel; the best he can do is to strike an average. Because so much of our investment in this country is speculative, there is all the more need for frequent reappraising of real estate. This is a thought that we should strive continually to bring home to institutional lenders.

CURRENT ECONOMIC PROBLEMS MAKE VALUATIONS DIFFICULT

There can be little quibbling over the fact that the times have never been more difficult in which to value property than they are at present. In 1929, according to Robert A. Doane, the wealth of the United States was 452 billion dollars, whereas in 1860, it was only 20 billion dollars. The rate of increase compounded annually was 4¾ per cent. Now, if this increase had kept up, in 1944 our wealth would be 903 billion dollars, and in 1959—just twenty years from now—it would be 1,806 billion dollars.

The world has known nothing like the increase in the wealth of this nation from the years 1860 to 1930, a span of seventy years. Pareto[1] has pointed out that in the 226 years from 1660 to 1886 the wealth of the United Kingdom increased from 8 billion francs to 235 billion francs, or at the rate of 1½ per cent. From 1886 through 1929, the increase in wealth was also at an annual compounded rate of about 1½ per cent. Pareto states further: "One may infer from that that only by exception can wealth increase in a geometrical progression equivalent to or exceeding a rate of 1.02 per cent or 1.03 per cent."

One of the causes of our economic troubles lies in the fact that over the period of all the years mentioned, both in Great Britain and in this country, the average rate of interest was over 4 per cent. If wealth increases at the rate of 1½ per cent and a safe interest rate of 4 per cent is established, it stands to reason that economic maladjustment ensues. What happened and what continually happens is that capital is being continually destroyed by obsolescence, the replacement of industries, wars, and like factors. Just a few short years ago railroad bonds were selling with a yield of 4 per cent to 4½ per cent with maturities of one hundred years and more. But 100 years ago, there was not a railroad system in this country, and it is possible that there will not be any in the year 2039. For the past 300 years the secular trend of interest has been downward. We, as appraisers, must not only be cognizant of long-term trends but of short-term variations which may run contrary to the general trend.

Appraisers must accustom themselves to the fact that to date we have not even begun to get below the surface of the science of valuation. What was right yesterday may be wrong today; and what seems true today may prove untrue tomorrow. Therefore no one can afford to be dogmatic.

Previous mention has been made of that sixth sense which so many appraisers of the old, nonscientific school have been accustomed to use. Everyone laughs and jibes at the horseback or windshield school of appraising. The old horseback appraiser had faults, but, in spite of the fact that he could not use formulas and stick to rules, he had, more often than not, good common sense. He was not trained to express his thoughts; and those words and thoughts which he found difficult to express he called his sixth sense.

But now to analyze his common sense! Of what did it consist? Well, he knew costs roughly; he knew income roughly. Also he knew neighborhood trends, and his so-called sixth sense was the sum total of his experience in the economic world, which was just about as good as the service rendered by many outstanding stock-market counselors today. (Incidentally, if anyone wishes to know how good were such services as Babson's, Brookmire, Gibson, Howard, Moody's, or Standard Statistics for many years prior to 1929, the July, 1936, issue of *The Journal of Business* of The University of Chicago provides not only interesting but startling data on this subject.) Think of the appraisal and investment advice given us by bankers during the past two decades! It indeed may be said that the appraiser compares most favorably with some of those great analysts.

The three principal methods used in valuation procedure — cost, market data comparison, and capitalization—have been reviewed briefly. They are all useful, but only too often are values arrived at by throwing each of these three methods into a hat; a bit of pepper and salt in the way of description, rent rolls, and photographs are then added in order to spice this concoction; the result is then shaken thoroughly as one would mix a cocktail—and lo!—what have we? An appraisal!—which is then brought out and placed between two beautifully gold-embossed covers.

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[1] Vilfredo Pareto, *The Mind and Society* (New York, Harcourt, Brace and Company, 1935), Vol. IV, §2316, p. 1664.

The old codgers of bygone days have received many laughs, but the average appraiser of today frequently goes through a lot of hocus-pocus—quite seriously, of course—which is no sounder scientifically than were some of the methods of yesteryear.

NEW APPROACH NEEDED

If we are to progress in our valuation procedure, we must acquire a new approach—a fourth dimensional approach, it may be called—which involves an understanding of the fundamental economic factors involved in valuation. Our foundations of value are different today than they were a decade ago, and there is little doubt but that the economic scenes surrounding us are changing rapidly at the present time.

Those who must reach decisions of importance in the economic world—and that includes the appraiser—must have a perspective beyond that of the ordinary man for it is this capacity which will determine ability to measure the future in the light of the present and past.

Personal observation is not enough; our vision becomes myopic and creates illusions. Because the problems which have beset us during the past ten years have been so staggering, we cannot throw up our hands in blank despair. Rather must this sequence of events create a greater challenge which appraisers must be prepared to meet.

Too many of us are ignorant of how our society functions, and most individuals are awed by the complexity of the problems involved. So it may well be asked: How can we know what these fundamental problems are? And how can they be understood?

The field of economics is large, and the ways in which the processes of trade, money, banking, finance, tariffs, and taxations affect real property are many. Even in our own restricted area we must know more about the supply and demand for housing, mortgages, interest rates, national income, population movements, changed demands for various types of space, transportation, purchasing power, building costs, the real estate cycle, and many other constants and variables too numerous to mention. Also, today we seem to live in a world of broken promises. Internationally we have walked a very crooked road from Versailles to Berchtesgaden. Governments since time immemorial have made promises relative to money, yet with one exception — ancient Greece — practically every government in the world has at one time or another debased its currency. Hence the old term "money changers," who were the valuation experts of money in their day! In real estate we have seen, and see today, promises made to repay debts—mortgage debts—which, incidentally, pyramided in our urban cities from 18 billion dollars to 36 billion dollars in the ten years from 1921 to 1931. These promises, in many cases, can never be fulfilled. Promises are the foundations upon which modern mankind and modern civilization live, and as we value our real estate we must also measure the worth of the promises and contractual relationships which are today an integral part of our system of property ownership.

Knowledge of all these things is the fourth dimension which we need in appraising. Without knowledge, to a greater extent than ever before, we shall be doomed to failure in our calling. Rare is the individual who is so gifted that he may discern the regularity and the cadence of dynamic and conflicting economic forces; but all appraisers must strive with all the powers they can command to perceive the movements and the patterns of economic behavior.

One thought more. Property owners, bankers, and institutions have turned to us—to all appraisers—in despair; they hoped that we would and could become the magicians who would make the impossible become possible. The position of those who invested and loaned at superstratospheric price levels is similar to that of the masses of whom Peter Drucker has recently written in that most worthwhile volume, *The End of Economic Man.*[2] He states: "If you are caught between the flood of a past, through which you cannot retrace your steps, and an apparently unscalable blank wall in front of you, it is only by magic and miracles that you can hope to escape. 'Credo quia absurdum,' that cry of a master who had known all the bitterness of deepest and blackest despair, is heard again for the first time in many a century." And we appraisers are asked to furnish the values — and the magic — in order to lessen the despair.

Indeed our task is most difficult; of that there is no doubt. However, the only way we can meet the future is by being so honest that it truly hurts. We cannot be afraid to turn our backs on the past and say that something has no reasonable value, even though people may be buying that very thing which to us may seem to be worthless. Issues cannot be straddled. And neither are we alchemists; we are merely technicians who must be just as cold as is the laboratory technician himself.

Poor appraisers and good appraisers cannot live side by side. Like Gresham's law, the poor drive out the good. Therefore, we must fight the fight of education both for our unselfish and selfish good.

The pressure of public opinion on us today is terrific. Our heritage is one of increasing values, plus our American instinct known as speculation, and the compulsion and urgency is to stretch values—get them up—get them up— and get them up more! Every appraiser is faced with unemployment if he does not give what is wanted because the tendency is to hire those who will produce the desired results.

As against this, there is only one weapon, and that is integrity. The battle may be long, and the belt may have to be hitched in a few notches; but if we cannot win in our generation, we at least shall know that we have left behind us a better heritage for those who come after us than we ourselves received.

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[2] Peter Drucker, *The End of Economic Man* (New York, John Day Co., 1939).

WHAT MAKES THE HOT SPOT "HOT"?

Joseph B. Hall, M.A.I.

When two insulated electric wires carrying current cross, nothing happens. When two arteries carrying traffic are separated by a grade crossing, nothing happens. The flow is uninterrupted. Remove the insulation, and you have heat caused by the short circuit. Remove the grade separation, and usually a "center" develops. If the traffic is of the right character, a *hot spot* is created.

CONVENIENCE

Why do we have heavier traffic flow at certain points? Convenience is the answer. Rivers originally were the main arteries, the most convenient. Where two rivers met—where traffic converged—a hot spot developed. Pittsburgh is an example of this. Where river and lake met, Chicago developed. Convenience of transportation helped in the establishment of towns.

When railroads developed, they followed the paths of least resistance, the most convenient locations—level ground, along rivers, through passes in hills and mountains. Rail transportation became more convenient, so rail centers became more important than river towns. Where railroads crossed, towns frequently developed—hot spots attracted by two flows of traffic.

So cities developed due to convenience—convenience of transportation, convenience to raw materials, convenience for protection. At the start, the cities clustered around the trading post or store. This store was the hot spot of the town. All roads led to the center of the town where the store was located. The very construction of the roads made the center most convenient.

With the development of cities, more stores were constructed at the center, and the people began to build farther and farther out. Many towns developed like a wheel with a series of spokes leading out from the center. Detroit and Chicago have diagonal streets which lead from the center, representing old roads which have become main arteries. Many of these old roads have disappeared, but sections of them still exist, as Vincennes Avenue in Chicago.

With the increase in size of cities, it became inconvenient to go downtown for everyday purchases. Neighborhood stores developed, mainly food stores. Food was bulky, and it was more convenient to buy it close to home. The downtown area was still more important. It required less population to support food stores than furniture stores, department stores, wearing-apparel stores, and others. The downtown area still was most convenient to the mass of people required for the support of such stores. Concentration of population through convenient transportation made these central business sections the hot spots.

As cities developed further, transportation facilities were extended. Surface lines covered towns with a network of tracks, intersecting at many points. Certain of these intersections were convenient to large areas of population. The retail areas expanded at these points since they were more convenient to certain groups of people than the downtown areas. The distances to the central business area had become greater with the growth of the city. More time was required—more inconvenience. Central areas still continued in importance since they still represented the most convenient point for the entire city and the concentration of population required for certain types of retail trade. The convenience of transportation made the downtown sections desirable for offices, semiwholesale concerns, and certain types of light manufacturing. This concentration of buying power helped maintain the importance of downtown areas.

DEVELOPMENT OF OUTLYING BUSINESS DISTRICTS

Where the downtown area was most accessible, there was less reason for the development of important outlying areas. Toledo, with good accessibility to the downtown area, has few important outlying areas. Cincinnati, with its arteries wending through the hills to the downtown areas, has few highly developed outlying retail districts—the presence of the hills and absence of many cross-town arteries makes the downtown area more convenient. Pittsburgh, on the other hand, has seen the development of outlying areas since the hills plus the rivers have made it difficult for the mass of population to reach the downtown section. The size of Chicago has brought about the development of many outlying business areas of considerable importance.

Convenience has been stressed. Is this an important factor? A survey by the Scripps-Howard Newspapers furnishes the answer of over 53,000 housewives to the question, "Why do you trade most frequently with this grocer?" (It may have been an independent, corporate chain, or supermarket):

Convenient location	27.2%
Best quality	15.5%
Best values	13.9%
Lowest price	12.2%
Complete stock	7.0%
Delivery service	5.6%
Store conditions	5.1%
Charge account	4.8%
Other reasons	4.9%
No reason	3.7%

Convenient location ranks first, with 27.2 per cent of the votes. A survey by the Kroger Grocery & Baking Company in five cities showed convenience as the reason given by 70.5 per cent of those interviewed for shopping at certain stores for food. The fact that food, a bulky product, was involved accounts for the high percentage.

Convenience develops the hot spot. The degree of heat depends upon the concentration of buying power. Ten thousand volts are hotter than one hundred volts. Ten thousand people develop hotter spots than one hundred people.

Shopping areas convenient to apartment sections usually develop higher values than those adjoining single-family developments. The downtown area, the center of various converging transportation facilities, still "is the spot most accessible to the greatest number of consumers," as stated by Richard U. Ratcliff in *The Journal of Certified Property Managers.*[1] This article states further:

> "Two authoritative studies of retail trade, one covering Baltimore in 1929 and the other Philadelphia in 1935, reveal the relative importance of the central area. In Baltimore, the central shopping district contained 6.1 per cent of the city's stores and accounted for 28.1 per cent of the total retail business. In Philadelphia, the corresponding ratios were 9.2 per cent and 37.4 per cent. In only two retail classifications did the central district account for more than 40 per cent of the city sales — the general merchandise group with 71.5 per cent and the apparel group with 63.2 per cent. In three other groups, the central area accounted for roughly one third of all sales—the furniture-household group, the restaurant group, and the unclassified group. Twenty-five per cent of all drugstore sales, 15 per cent of the sales of the lumber and building-hardware group, and less than 10 per cent for the food stores, automotive group, and filling stations were made in the central area."[2]

TRAFFIC

The degree of "heat" in electricity is measured by a voltmeter; in a hot spot, by traffic counts or rentals paid. No attempt will be made here to describe the various types of traffic counts and the importance of the characteristics of the traffic as compared to mere quantity. We are interested more in the causes than the results of those causes.

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[1] Richard U. Ratcliff, "The Selection of Tenants for Retail Locations," *The Journal of Certified Property Managers* (Vol. IV, No. 4, June, 1939), p. 344.

[2] Ibid., p. 345.

The problem of convenience and concentration of buying power becomes involved as the methods of transportation change. Most cities were built for horses and wagons and streetcars, not for rapidly driven automobiles. In the days of fewer automobiles and less speed, the streetcars furnished the major form of transportation for most cities. Traffic flowed fairly smoothly. Retail areas developed at convenient locations. Intersections of important lines developed higher values due to concentration of buying power.

Any interruption in the flow of traffic affects convenience and the resulting values. Streetcars, when once boarded, could be ridden downtown with little inconvenience except additional time. When automobiles came into use, the picture began to change. Most streets were not built for fast-moving automobile traffic. The rapid increase in the use of automobiles resulted in congestion and hazards of driving. You do not worry about what happens to the streetcar after you alight from it, but you do worry about parking facilities for your automobile and the cost thereof. The increased use of automobiles is indicated by the following figures furnished by the Transportation Commission of the city of Cleveland. They represent the number of persons entering and leaving the downtown area on the average weekday between 5:30 A. M. and 9:30 P. M. The figures for streetcars since 1928 include busses operated by the Cleveland Railway Company.

	STREETCAR		AUTOMOBILE		TOTAL
1922	466,875	67%	228,232	33%	695,107
1924	404,057	55%	329,759	45%	733,816
1926	387,609	54%	336,754	46%	724,363
1928	374,015	49%	367,634	51%	741,649
1930	339,155	45%	392,140	55%	731,295
1932	267,389	41%	382,830	59%	650,219
1934	302,859	43%	398,674	57%	701,533
1936	348,888	42%	473,917	58%	822,805

While some inaccuracies may exist, the size of the group eliminates their effect. The basis for the count was the same in all years.

The effect of automobile traffic is demonstrated. It increased from 33 per cent in 1922 to a peak of 59 per cent in 1932 and has continued at about that level. No figures are available for 1938, but studies made indicate totals approximating those of 1936. Streetcar and bus traffic declined steadily from 1922 to 1930 in spite of the total remaining somewhat the same. Automobile traffic in 1936 exceeded the streetcar traffic of 1922. These figures clearly show the problems presented by increasing automobile traffic.

The increased use of automobiles is changing the character of retail areas. Convenience is the important factor. Mr. Ratcliff's article states, "Thus the differential productivity of various retail sites arises from the differences in the aggregate amount which various consumer groups are willing to pay for convenience in the purchase of various articles."[3] If the downtown areas become more inconvenient or, conversely, if the outlying shopping areas become more convenient, values in the downtown area will be affected. The hazards and strain of driving on crowded streets and the expense of parking work as disadvantages to downtown areas. Conversely, the ease of reaching outlying areas is an advantage.

RENTALS

Following are ground-floor rental figures for an important corner in a large midwestern city for four selected years:

1928	$152,000
1931	$122,000
1935	$ 67,000
1939	$ 78,500

Maybe this drop was due to the depression—maybe it was due to greater convenience of outlying areas accessible to automobiles. However, rentals in many outlying areas have not declined. A recent extensive study of retail values in this same city disclosed that ground-floor rentals do not exceed 50 per cent of the rentals in force ten years ago. There are two or three outlying centers, where concentration of consumers was due mainly to streetcar transportation, that have shown similar drops. Other outlying areas have developed and shown fine improvement during this same period.

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[3] Ibid., p. 350.

FOOD STORES AS EXAMPLE

Let us view the changes in these outlying districts from the viewpoint of the retail food business. Food products, as stated above, are bulky. Automobiles and improved refrigeration have influenced the food business. People no longer have to carry bulky packages long distances. They carry them to their automobiles and drive home. The inconvenience of parking in downtown areas makes the food stores in these locations less desirable. The ability to maintain freshness through refrigeration makes frequent shopping less important. Approximately 50 per cent of food buying today is concentrated on Friday and Saturday. So we find changes in outlying areas.

As has been reiterated in this article, convenience is important. Before automobiles reached their present use, the corner food store was important. It tapped the immediate area and made unnecessary the carrying of bundles for long distances. There were certain larger food markets at strategic points where buying power was concentrated, but food buying was mainly an immediate-neighborhood transaction. The automobile has changed this. Larger food stores have been developed where shopping is concentrated and parking available. The family piles into the car, in many cases, and goes on its weekly food-buying trip. The average sale per customer in these stores is much higher; they are "pantry-stocking stores" as compared to the "neighborhood pickup stores."

Following are some figures based upon studies made by the Research Department of the Kroger Food Foundation in certain cities:

TYPE OF STORE	PERCENTAGE OF STORE SALES IN VARIOUS ZONES		
	0-¼ Mile	¼-¾ Mile	Over ¾ Mile
Isolated	70.4	14.8	14.8
Minor	64.6	24.4	11.0
Intermediate	53.3	31.5	15.2
Major	34.8	34.8	30.4
Parking lot	23.5	42.0	34.5

These figures demonstrate the reliance of the isolated store upon the immediate neighborhood and the ability of the stores with parking lots to draw from larger areas.

The following tabulation shows the percentage of customers in these studies who came by automobile, also the percentage of business secured on Saturday:

	PER CENT BY AUTOMOBILE	PER CENT OF SALES ON SATURDAY
Isolated	20.7	39.6
Minor	30.3	41.4
Intermediate	34.7	42.5
Major	43.7	42.4
Parking Lot	56.9	52.6

It is interesting to note that a good percentage of the customers for the parking-lot store came on foot or parked outside the area checked.

These figures show the increasing use of automobiles and the need for convenient parking. Sales figures for the various types of stores would emphasize this even more since those with parking facilities frequently produce higher volumes. The average sale per customer is higher due to the ease of carrying the purchases to the automobile. One factor which has further affected such food stores has been the evening shopping hours which have made possible the use of the family automobile, otherwise occupied during the day by the husband in his business. More family shopping occurs in this type of store.

PARKING FACILITIES

Recently there has been more development of stores with parking facilities adjoining. Some of these have been isolated stores, others have been in a group development. The latter develops high values—a hot spot—due again to convenience. The customer can park once and complete her purchases, whereas in the isolated store she can supply only the needs catered to by that store. Some of the original "park and shop" developments did not provide sufficient parking. Others did not provide for space of sufficient size to accommodate present merchandising methods. It takes a proper balancing of these factors to produce a successful development. Where they have been properly constructed, they tend to pull business from the developed centers that are more inconvenient due to lack of proper parking facilities. The only answer for the older section is to provide ample parking. Sometimes this can be done. One has only to see the increase in parking lots in downtown areas to realize the efforts being made to make parking more convenient and thus to retain business. It would be well for all interested in this subject to read the booklet entitled, *The Parking Problem in Central Business Districts*, by Nolting and Opperman.[4]

It is simple to say that concentration of buying power makes the hot spot "hot." It requires a study of the various factors making this concentration possible to determine the soundness of any retail center. Automobiles have become one of the more important factors. And underlying all of these factors runs the one important element of convenience to the buying public.

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[4] Orin F. Nolting and Paul Opperman, *The Parking Problem in Central Business Districts* (Chicago, Public Administration Service, 1938).

THE SUPERMARKET

JAMES TURNBULL

UNTIL about fifteen years ago the old-style neighborhood grocery store was the sole retail outlet for groceries, meats, and vegetables. Since then several changes have taken place, with the supermarket emerging as the mode of today and leaving a great accumulation of obsolescence in its wake.

The neighborhood grocery store was superseded by the drive-in market, built in an "L" shape on the rear of a corner lot. This was outmoded by the larger store in the middle of the block, set back from the street to permit automobile parking on the front of the lot. This, in turn, was made obsolete by the supermarket which today enjoys most of the provision business in the southern California area.

The first supermarket was built about ten years ago. It had a floor area of 10,000 square feet or more. The structure was built flush to the sidewalk, with posts supporting the front wall and roof. Parking facilities were none too good. From this beginning there evolved the supermarket of today. It differs from its predecessor in that it has no interior posts and adequate customer parking facilities are provided; in fact, automobile parking is one of the most important features of the present supermarket.

The net effect of this transition has been to increase the normal lot area in a neighborhood business district. Lots twenty-five feet wide were at one time considered normal. Today lots fifty feet in width are inadequate for many retail uses.

THE DEVELOPMENT OF THE SUPERMARKET

Briefly, the causes of the evolution from the neighborhood grocery to the supermarket were: (1) price, (2) diversity of merchandise, (3) convenience of making purchases, and (4) merchandising acumen.

Perhaps price was the first and most important condition responsible for the technical advancement in provision merchandising. In this sense it might be said that the present-day market is a child born of the depression. This period was ushered in by an era of economic instability, as evidenced by diminished incomes and increased unemployment. Of necessity, people became price-conscious. Prices of foodstuffs were declining, and people traveled long distances to save a penny here and there. This tendency was stimulated by wide newspaper publicity concerning "loss leaders" and other inducements offered by the more aggressive merchants. In the Los Angeles area people are known to have traveled twenty-five miles to supermarkets to purchase a week's supply of provisions.

Civilization is a movement along the lines of least resistance. People trade at those places where the greatest number of objectives can be accomplished with the least expenditure of effort. The supermarket stocks from 3,000 to 4,000 items, as compared with from 600 to 800 in the old-style grocery store. Like the department store, the supermarket vends a diverse array of goods; unlike the department store, it has adequate free parking facilities adjacent to its place of business.

This highly integrated enterprise was able to undersell the older and smaller neighborhood grocery stores and made it easier for the public to buy cheaply. The effect upon the volume of the older enterprises is obvious.

Here it might be well to point out that

the supermarket is not entirely free from competition. In the past few years there has been developed the farmers' market in outlying areas where cheap frame construction is permissible and large parking areas are available.

The supermarket probably will continue to be popular. The latest promotional schemes contemplate the location of leading national chain stores in the district to stabilize it as a shopping area. In these developments a matter of major importance is the provision for adequate parking space, alongside or in the rear, which may involve an added capital investment of from $40,000 to $100,000 and is generally worth it.

Management is one of the most important conditions affecting the success of the supermarket. There are numerous instances in which a market failed under one management and prospered under another. There are many matters which affect all of the concessionaires collectively and items of expense which must be shared by all. Here the manager plays an important role in securing co-operation in the matter of joint advertising and in the sharing of common expenses, such as for janitor, parking-lot attendant, water, gas, electricity, etc. Without the correlating influence of a competent manager, chaos would reign and failure ensue.

Some markets are operated by one merchant who has several managers for the several departments, but in the majority of markets each concession belongs to a separate owner who is a specialist in his particular line. However, there appears to be a limit to successful operating diversification. Experience indicates that it is better to group the concessions in a few hands which are strong financially rather than to have a large number of small concessionaires who are financially unstable and who usually are not co-operative in the sharing of common expenses. Five concessions are customary: (1) meats and fish, (2) groceries, (3) fruits and vegetables, (4) delicatessen and beverages, and (5) bakery.

SELECTION OF LOCATION

All other conditions, such as management, being equal, location becomes the matter of paramount importance. By location is meant the position of the site with respect to human activities—that is, purchasing power. In any other sense location is meaningless.

The selection of a site for a supermarket should include an analysis of the neighborhoods surrounding the sites under consideration with regard to density of population, trading habits, and the degree of accessibility of the site to all of the people in the neighborhood. Of course, shoppers may travel long distances to reach a particular market, but the fact remains that when an equally desirable market is built closer, then their shopping will be done nearer home. This is why the eventual volume of business will come largely from the immediate neighborhood. And thus the immediate neighborhood is the matter of greatest concern.

In the selection of a site for a supermarket it is important to avoid heavily traveled arteries because of the difficulty of getting in and out of the market. Also, it is desirable to avoid areas largely improved with apartment houses because such residents have fewer mouths to feed and "eat out" a part of the time.

The environing conditions most desired in a site for a market are (1) a neighborhood which is fairly well built up with relatively new single-family residences occupied by mechanics and other nonwhite-collar working people and (2) an adequate amount of free parking space.

Areas of new residences are generally

preferable to the older districts because the income level of the people is usually higher. In most cases the areas occupied by workingmen have a greater percentage of children, the residents consume more food per person, and of necessity this class is generally more price-conscious.

PLAN AND ARRANGEMENT

Experience teaches that the ideal size of a supermarket structure is about 90 feet wide by 150 feet deep, built to the sidewalk. The front 105 feet of depth are used for selling space and display, the rear 45 feet for storage and working purposes. There should be a mezzanine floor, about 20 feet deep, across the rear of the store for offices. Rest rooms for the public are also necessary. There should be ample space in the rear of the building for trucks to unload merchandise and an adequate incinerator.

On one or both sides of the building there should be a vacant lot, paved with asphaltic concrete, for free parking of customers' automobiles. This parking space should be at least equal to the area of the market building, and preferably larger. The space should be at least 60 feet in width, marked with white lines to designate parking spaces, and arranged with a separate entrance and exit. There should be an attendant on duty on the parking lot from 4:00 to 6:00 P.M. each day, with all-day attendance on Saturdays.

Free parking space in the basement has been tried and proven a failure. So, too, has parking space across the street. The parking area must be adjacent to the store and have both good visibility and good accessibility; otherwise it will fail to serve its purpose.

The conventional arrangement of the various departments in the enterprise is usually as follows: The fruit and vegetable concession is along the sidewalk in the center front of the building, but not reaching to the side walls. Immediately in the rear of this, backing against it and facing the rear end of the store, are the liquor, beverage, and delicatessen concessions. These face the grocery concession, which occupies the rear central portion of the store space. The milk and butter refrigerator should be at the extreme rear of the grocery space; with such an arrangement the frequent purchase of these items requires customers to walk past other merchandise on display.

The meat and fish concession should occupy the space on the left side of the market (as the customer enters), extending from the sidewalk to the rear along the left wall; the bakery, ice cream, and candy concessions occupy the corresponding space along the right side wall, extending from the sidewalk toward the rear.

COST OF THE BUILDING, FIXTURES, AND EQUIPMENT

Many of the supermarkets are in a fire zone which prohibits frame wall construction. The custom has been to build with brick in these zones and also in others where the ordinance does not prohibit frame construction.

There follows an estimated cost of a typical brick structure, located in the Los Angeles area, with an open front, no interior posts, and an eighteen-foot ceiling.

Building			
Front, 90 ft. x 105 ft. in depth	$18,500		
Storage and workrooms in rear, 90 ft. x 60 ft., stucco over frame	7,500		
		$26,000	
Parking lot			
15,000 square feet of asphaltum pavement		1,000	
Total cost of building and pavement			$27,000
Fixtures			
Refrigeration plant, complete	$ 2,500		
Meat and delicatessen cases, grocer's shelving and island tables, fruit and vegetable stands, bakery display cases, all other necessary fixtures	10,000		
Total		$12,500	

Equipment			
Cash registers, meat grinders, bone cutter, slicing machines, coffee grinders, etc.	$ 7,500		
Neon signs, inside and outside	2,500		
Total		$10,000	
Total cost of fixtures and equipment			$22,500
Grand total—Building, fixtures, and equipment			$49,500

Several years ago it was the practice of the owner of the real estate to install all fixtures and, in many instances, the equipment, too. Today it is the custom for the owner to install the refrigeration plant, the necessary refrigerated storage boxes, neon signs, electric fans, and lighting fixtures. The tenant installs the fixtures and equipment.

The maximum useful life of fixtures and equipment is ten years. In fact, experience indicates that a period of seven years more closely approximates actual conditions. This short life is occasioned chiefly by the inordinate usage and also by obsolescence.

THE PERCENTAGE LEASE

The two forms of leases commonly used are (1) the percentage lease and (2) the flat-rental lease. A few years ago most of the market leases were of the percentage type; in recent years there has been a marked trend toward the flat-rental type of agreement. This is probably the outgrowth of the inability of the two partners in a percentage lease—the landlord and the tenant—to get along with each other.

The percentage lease, without a reasonable minimum rental or a recapture clause, is a poor lease for the landlord. Even though a reasonable rental is being paid at the time of the appraisal, the fact remains that this type of lease penalizes the value of the property. It is a matter of history that most supermarkets reach the peak of sales volume in the first three years after opening. Many such markets are today selling less than 50 per cent of the volume of five years ago.

Perhaps the principal reason for the decline in volume after two or three years is the development of competitive enterprises, either in the immediate neighborhood or several miles distant. By way of illustration, eight years ago a supermarket was opened in one of the newer, fast-growing residential areas of Los Angeles. At that time the sales of groceries were $50,000 per month; today the volume is less than $10,000. At that time there was no neighborhood competition; today there are several such markets in two adjoining blocks, competing violently with each other for business. The result is obvious.

There is a further reason for the decline. It is the development of competitive enterprises in other areas. Formerly, people from the sparsely settled, distant neighborhoods would trade at the afore-mentioned market; today similar markets are found in these distant neighborhoods, and a part of the trade has migrated to places of greater accessibility and convenience. This condition is always possible.

The appraisal of a supermarket which is leased upon a percentage basis is one of the most difficult problems encountered by the appraiser. It is necessary that his investigation extend to distant areas for the reason that such areas may exert a greater potential influence upon the subject market than conditions in the immediate neighborhood.

THE FLAT-RENTAL LEASE

The flat-rental type of lease is one in which the rental is agreed upon for the full term of the lease. Under existing conditions, this is usually for ten years. Several methods are employed to indicate the amount of the flat rental. Those generally used are (1) the compartaive approach, in which the rental is indicated by prevailing rentals in the area; (2) the interest on the investment approach, in which the suggested rental would be that amount sufficient to show a fair net return on the investment; and (3) the percentage approach, in which the rental is based upon percentages of the estimated gross volume of sales.

In the last-mentioned method an estimate is first made of the volume of business which may be expected. For illustration, analysis and experience may indicate the following reasonably expected sales volumes:

Meats	$ 8,600	per month
Groceries	$17,500	" "
Vegetables	$ 7,100	" "
Delicatessen and liquor	$ 4,400	" "
Bakery goods	$ 1,750	" "

Experience indicates the following rentals, expressed in terms of percentages of the gross sales, as reasonable in those cases where the refrigeration system and iceboxes are installed by the landlord. (These usually cost about $3,500.) The other fixtures and equipment are installed by the tenant.

MONTHLY SALES	RENT
Meats	
Under $3,000	5%
$3,000 to $5,000	4%
$5,000 to $10,000	3½%
$10,000 and over	3%
Groceries	
Under $5,000	4%
$5,000 to $10,000	2½-3%
$10,000 and over	2%
Vegetables	
Under $2,500	5%
$2,500 to $5,000	4%
$5,000 and over	3½%
Delicatessen and liquor	
Under $1,500	5%
$1,500 to $3,500	4%
$3,500 and over	3½%
Bakery goods	
Under $600	7½%
$600 and over	5%

It is seen that the percentage of the gross income available for rent decreases as the volume of sales increases. This is necessary because the larger volume is attained largely by reason of lower prices and lower costs of doing business.

From this schedule of typical rental percentages, the flat rental can be estimated as follows:

CONCESSION	SALES	RENT	RENT
Meats	$ 8,600	3½%	$300
Groceries	$17,500	2%	$350
Vegetables	$ 7,100	3½%	$250
Delicatessen and liquor	$ 4,400	3½%	$150
Bakery	$ 1,750	5%	$ 85

These figures are typical of a number of markets in the Los Angeles area.

EXPENSES

While the overhead costs are borne by the tenants in most cases, they are here shown as a matter of interest rather than of pertinence. In one of the larger supermarkets in the Los Angeles area the actual average monthly overhead is as follows:

Refrigeration	$ 65
Lights	190
Gas	31
Water	20
Garbage disposal	16
Janitor	115
Bookkeeper	80
Parking-lot attendant	25
Sundries	25
Total	$567

To the above must be added other variable items of expense, such as repairs to the refrigeration system, equipment, and incinerator, contributions to charity, etc., which will average $100 per month.

In addition to the foregoing is the expense of advertising. The larger and more active operators spend as much as $600 per month for publicity.

These are the more or less co-operative expenses which are prorated among the various concessionaires or departments. The actual operating expenses of the various departments are not included.

EFFECTS OF COMPETITION

Within the past ten years there have been built about 350 supermarkets in the Los Angeles metropolitan area. At the present time about 10 per cent are closed; in about 25 per cent of the markets the landlord has reduced the rental from that stipulated in the lease, with the result that the lessee is now able to earn a meager wage; in about 25 per cent the tenant is continuing to pay the rental originally provided for in the lease and is on the verge of bankruptcy in doing it; and in the remaining 40 per cent both the landlord and the tenant are doing well.

In the early years of these markets the owner of the property installed all fixtures and equipment, even to the butcher knives. Many owners recaptured the entire investment, in rents, during the first three years. Such conditions may never again be known.

The old adage that "inordinate profits breed ruinous competition" applies to supermarkets as well as to all other ventures. Profits invite competition, and competition is the great leveler of incomes. When huge profits are to be made, then there are always large amounts of capital available to reap the harvests. The inevitable competition shears off the excess, and usually more.

The history of rental incomes from markets should serve as a red flag to curb the imagination of the appraiser. The indisputable fact that a market produced an average annual rent of $20,000 per year over the past five or ten years is no warrant for the assumption that this will be the average annual income in the future. The appraiser should "let the past bury its dead," and think in terms of what the future holds.

AN ACTUAL APPRAISAL

The figures from an actual appraisal report covering a supermarket located in Hollywood, California, are shown in the following.

Pertinent Data

Structure erected and equipped by fee owner seven years ago. Leases were made seven years ago for a ten-year period and have three years of unexpired term.

Flat rental provided for in lease	$20,400 per year
Lessee pays for utilities, upkeep, and repairs.	
Lessor pays taxes and insurance which amount to	$ 2,590 per year
Current rental value of premises if new leases were to be made	$12,000 per year

Summation Cost New

Land	
165 feet x 200 feet, market value today, if vacant	$ 90,000
Building	
80 feet x 105 feet, brick, cost new today	22,000
Parking-lot pavement	
85 feet x 200 feet plus 80 feet x 50 feet in rear of building—asphaltum pavement	1,200
Fixtures, installed by fee owner, if new today	12,500
Equipment, installed by fee owner, if new today	5,000
Grand total—Cost new today	$130,700

Depreciated Reproduction Cost

Land		
165 front feet		$ 90,000
Building—7 years old		
Cost new at current prices	$22,000	
7 years @ 3% = 21% depreciation 21% of $22,000	4,620	
Depreciated cost		17,380
Parking-lot pavement		
Cost new at current prices	$ 1,200	
7 years @ 3% = 21% depreciation 21% of $1,200	252	
Depreciated cost		948
Fixtures and equipment		
Cost new at current prices	$17,500	
7 years @ 10% = 70% depreciation 70% of $17,500	12,250	
Depreciated cost		5,250
Depreciated reproduction cost		$113,578

Capitalized Value

Net Income Expectancy—Next Three Years

	Per Year
Gross income expectancy of owner under present lease—3 years	$20,400
Expenses	
Taxes $2,512, insurance $78	2,590
Net income before amortization	$17,810
Less interest on and amortization of fixtures and equipment:	
Interest @ 10%, amortization at 10% 20% of $5,250, the depreciated cost	1,050
Net income to land and building, before replacements and amortization	$16,760
Less periodic replacement each 10 years, roof recover, etc., estimated	300
Net income to land and building before amortization	$16,460

Net Income Expectancy—After Three Years

Gross income expectancy of owner after 3 years—on new leases		$12,000
Expenses (as before)	$2,590	
Fixture and equipment charges (as before)	1,050	
Replacement item (building) (as before)	300	3,940
Net income to land and building before amortization		$ 8,060

Computations

Present worth of net income	
Next 3 years @ 9% $16,460 x 2.531	$ 41,660
From 3rd to 26th year @ 9% $8,060 x 7.398	59,628
Present worth of land reversion @ 6%	
Value assumed $90,000 $90,000 x .22	19,800
Total	$121,088

Recapitulation

Capitalized value of land and building	$121,088
Add for depreciated cost of fixtures	5,250
Total	$126,338
Deduct for replacement of fixtures and equipment to perpetuate income	12,250
Capitalized value of property "as is"	$114,088

Comparison of Estimates

Summation cost new	$130,700
Depreciated reproduction cost	$113,578
Capitalized value	$114,088
THE VALUE REPORTED	$114,000

HAS LAND A VALUE?

LEONARD C. SMITH, M.A.I.

MANY of the ills to which the appraising of real estate is subject find their inception in the efforts of appraisers to estimate the value of land. Value has been defined broadly as "the present worth of all of the rights to future benefits arising from ownership." To the appraiser the measure of that value is the future use or usefulness to a typical user. The fact that a future use is contemplated makes necessary a prediction as to the nature, extent, and intensity of that use, and there the appraiser's troubles multiply.

WEAKNESSES OF TERM "HIGHEST AND BEST USE"

In the conventional appraisal process the value of land not in use is estimated as if improved to its "highest and best use." This term, like virtue, is more relative than specific. It offers a vague description of an abstract condition rather than the measure of a fact. When the appraiser renders an opinion of the value of land "as if improved to its highest and best use" without stating a definite program of use, the validity of the appraisal is questionable. It is like signing a check for a stated sum and failing to enter the name of the bank upon which the check is drawn.

There are other related weaknesses which appear to be inherent in many appraisals and which will bear some discussion. Even if the appraisal report states the specific use upon which the appraisal of the land is predicated, the conclusion of value may remain subject to considerable doubt. Where the plan of use which is predicted to reflect the indicated value in the subject land is purely hypothetical, it is usually considered without regard to the potential use of similar environing lands or to the competition which might be afforded by their development. If a given district were definitely in need of one parking lot, and not more than one, and ten appraisers were each to appraise simultaneously in the conventional manner a different but suitable site, the ten estimates of value would be predicated upon a use which would be impossible, or in any event highly improbable, for at least nine of the sites to attain. An honest and qualified opinion of highest and best use is applicable only to the conditions of the moment of appraisal and disregards the possibilities of the future so vital to the appraisal.

"PRODUCTIMUM" USE

The term "highest and best" in itself is loose, indefinite, and confusing. A number of instances have come to light among real estate men—surely not appraisers!—where highest and best use was thought to refer to the height limitation imposed on the land by the zoning or building ordinance! Appraisal terminology should include a better, one-word term to apply to that condition of land utilization which is deemed to bring the site to its productive maximum. *Product*ive max*imum* suggests the term "productimum," and the expression "productimum use" is offered for consideration in lieu of "highest and best use" or "optimum use." However, by any name or description, the prediction of the most profitable or beneficial use of land would be just as hazardous and difficult.

That there is a "productimum" use for every parcel of land is patent, although, in many cases, such use would appear to be negative—that is, the land to remain idle. It is the task of the appraiser to reach a conclusion concerning such use before attempting an estimate of land value. The value of land is potential and is a function of the effectiveness of use. The appraiser's opinion of "productimum" use is conclusive in the measure that it results from consideration of a described condition of specific use rather than from a prediction of abstract potential use.

A valuation estimate which is predicated upon indefinite potential usefulness evidences nothing more than an abstract concept of value and is too limited by circumstances to be called an appraisal. An excellent analogy is to be found in a lumberyard. A pile of dimension lumber—say, two by ten inches by fourteen feet long—is awaiting use. The lumberman is offering it for sale at a price which is governed by supply and demand in the open market. The real value of the lumber in the economic concept depends upon the use to which it will be put. The potential uses are many. The lumber might serve as framing for a small bungalow, a store, an apartment house, a factory, a bridge, a ship, etc. It might be needed for ordinary runway planking. Some enterprises might use it profitably as material for seats in a grandstand. The lumber may have provided great utility as part of a grandstand; after that need has passed, it might be used in the construction of a house and have a different value. If it were to remain unused and in the open indefinitely, it would become unfit for one after another of its potential uses until finally only its value as fuel would remain. But in every case, its value would depend upon the means and time of its employment.

Land may be viewed in the same category as the lumber. Its potential uses may be many, but once it has been dedicated to a specific use, its value-producing capacity is limited to the like capacity of the development of which the land is an integral part. Land achieves value status if, as, and when it is incorporated into a benefit-producing form. It would be quite as reasonable to impute a certain portion of the value of a building to the plumbing or the brick as to attribute part of the value to the building and the remainder to the land. The fact that land remains after the economic life and even the physical life of the building has expired does not entitle it to any different treatment in appraising than the salvage material remaining in the building. We know that the material substance that makes up the land will persist indefinitely, but the extent of the value-producing attributes which the land might have in the distant future continues to be exceedingly conjectural. The separation of value estimates into amounts for land and for improvements is a relic remaining from the unholy past of the unqualified summation appraisal. It is a practice that is confusing, ineffective, and difficult to substantiate.

SENIORITY ADVANTAGE

An important factor that enters into many appraisals arises from the fact that a specific use of land tends to draw upon the surrounding area in supplying a particular need to the extent that owners of adjoining lands may be precluded or at least discouraged from attempting to enjoy a similar plan of use. This might be called the "seniority advantage." Any value arising from it certainly should not be imputed to the land but to the combination of the use and the land. Whenever profits from seniority advantage become excessive, competition usually enters in to reduce the profit and to share the benefits of such advantage. It often remains, nevertheless, an effective deterrent to competition.

Many times seniority advantage is disregarded, and competition in the same plan of use develops to the impairment and even the destruction of part or all of the value. This illustrates another eventuality which is not contemplated in valuations predicated upon the customary application of the concept of "highest and best use."

HOW SHALL LAND BE APPRAISED?

If the appraisal of land with or without a stated program of use is questionable, by what means and upon what basis is land to be appraised? The thought that land alone has no value will bear considerable reflection. Without question any specific usefulness of land may be valuable, but it would appear that any value which arises from such use should be imputed to the development which embraces the land and is able to extract utility from it. It is the combination or the union of the land with the program of use which is responsible for the value. It is a function of an appraisal to provide an estimate of the nature and extent of the value which is evident or predicted under a specific plan of use.

It should be admitted readily that it is difficult to imagine a parcel of land anywhere at any time that would not command some amount of goods in exchange however small and therefore be considered to have value at least in the economic sense. This assertion is entirely consonant with the concept that the land itself has no value. When a man pays a price for land that appears to have no potential use, he is not paying for the land but for one or both of two reasons: The land offers a use which would be peculiar to him, or he believes that there are speculative possibilities that the land will acquire potential use in the future. Either eventuality is beyond the realm of consideration of value to a typical user.

If the estimated income from a definite program of land use provides a return on the investment in the enterprise in excess of that which would be considered commensurate with the risk involved, why, as in a land residual capitalization, should the excess of income be imputed to the land as reflecting an increase of land value over its value by comparison? Would it not be more logical to attribute such excess to the tenancy which has provided the fortunate plan of use of the land? The excess, then, may be considered in the light of the risk of its continuation and of the probability that it would inure to the benefit of a typical user. Such a practice would obviate the frequently untenable position in which the appraiser is found when the land residual method of capitalization reflects a land value far in excess of the market price of adjoining lands just as desirable and suitable for the same use.

Under given conditions land will join with improvement to produce a certain reflection of value, but if there is a change in conditions, in improvement, or both, a different value may be indicated. The land under a building is as much a part of the improvement as is the brick, lumber, plumbing, or any other portion of the structure and is just as inseparable. The conclusion is manifest that land in use should be treated as a component of the enterprise with which it is merged and that idle land cannot be valued in the absence of a specific plan of immediate use.

There is a growing conviction among appraisers that land enters into all three categories of economic goods, namely, consumers' goods, producers' goods, and service goods. As consumers' goods, it is used for the development of single-family homes and their adaptations. As producers' goods, it is used as a part of commercial and investment properties. As service goods, it is employed in providing parks, streets, and for other public purposes. A parcel of land may partake of the attributes of more than one category. The application of this concept of land exerts a profound effect upon the appraisal of land. It tends to make all the more difficult and hazardous the valuation of land as if improved to a hypothetical use. If land is to be considered in this light, the problem of its "productimum" use and the value under such program of use becomes very complex. Any attempt at a solution depends for its effectiveness upon a realistic approach, voluminous data, and a reduction of the process to the greatest simplicity possible.

CURRENT MARKET PRICE

It would be logical to consider at this point how a land appraisal may be made if land has no value. Land always has its price in the open market. It may be treated in a manner similar to any commodity in the marts of trade. But the question may be raised: How can land have a price and yet have no value? Admittedly, price indicates value, but it is value to an individual and generally does not contemplate improvement to the "productimum" use. The individual's price of idle land may be founded upon circumstance, caprice, ignorance, or sentiment and may bear no relation to any specific plan of use. The attributes of value are reflected in price data, but only in the proportion that the lands on which prices are reported bear to all the lands in the area under consideration. It is only when price information approaches a reflection of mass reaction in the area concerned that value to a typical user is indicated. Such a condition is rare indeed. In the preponderant number of requests for the appraisal of idle land, it is an estimate of the "currently obtainable market price," and not an appraisal of the "value," that is desired by the client and more nearly meets his needs. An appraisal of the *price* as of a given time may be made after consideration of adequate data, and such an appraisal will provide a far more rational and qualified conclusion than a value estimate based upon a hypothetical improvement.

SUMMARY

It would appear that the following concepts merit more intensive consideration on the part of appraisers:

1. An appraisal of the value of idle land must be predicated upon a specific plan of immediate use.
2. Any separation of the value of improved property into amounts for land and improvements should be discouraged.
3. Abolition of the term "highest and best" use and the adoption of a term which is more concise and descriptive would be desirable.
4. The effect of "seniority advantage" in an appraisal of the value of idle land and land in use should be considered.
5. The effect of the economic concept of land being consumers', producers', or service goods enters vitally into every appraisal.
6. The practice of offering an appraisal of idle land upon the basis of current market price rather than upon the basis of value to a typical user should be encouraged.
7. It is the specific usefulness of land and not the land itself that has value.

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APPRAISAL OF DEPARTMENT STORES

JOHN R. HOYT, M.A.I.

THE problem of appraising a department store involves more than simply the valuation of an improved piece of real estate. The department store is more of a business problem, though it is necessary to have sufficient collateral in the real estate—land and building—to conform to the legalities of the loan when the appraisal is for mortgage-loan purposes.

ANALYSIS OF STORE'S BUSINESS

In the suggested approach to the appraisal problem, the type of store is the first value factor to analyze. For example, a store like R. H. Macy & Company, which sells only for cash, would require a different treatment from a store like B. Altman & Company of New York or Marshall Field & Company of Chicago, which cater to a different clientele and sell on credit. Also, the reputation of the store in the trade is important, and this factor must be carefully investigated.

Next would be a study of the location, size of the property, neighborhood and neighborhood facilities, and the character and availability of transportation. The location must be analyzed as to the buying power present, the territory from which the store draws, and the competition it has to meet in its territory. Successful department stores are usually easy to reach and have a diversified and extensive trade territory. Good department-store locations almost invariably attract other department stores; hence the factor of competition is always present. It is also true that such grouping brings additional business.

The history of the business must be carefully analyzed—when it was established, how long it has been in its present location, how many times the store has moved since it was first organized, and the reason for such moves. A history of annual gross and net earnings is essential; such figures must be broken down to see what changes occurred in the expenses as the gross changed from year to year and the reasons for such changes. Many of our important department stores are establishing branches in the suburbs with apparent success; therefore, the branches of the subject property must be analyzed, their history of earnings, and what they are contributing to the general business of the company. If the subject property has no branch stores, inquiry must be made as to why not and also as to whether it would be desirable to establish one or more such branches and, if so, in what locations.

The delivery service of department stores is an important factor in retaining customers' good will, and an examination of this service should be made as to its efficiency, the area served, and the possibilities for improvement, all of which have a bearing upon the business potentialities and continuity.

VALUATION OF THE REAL ESTATE

The valuation of the property, as limited to the real estate, should be carefully made, both upon the cost or investment basis—that is, land value plus the building at the reproduction cost less depreciation and obsolescence—and the economic basis for the property as a whole, based upon actual or estimated current rental values for the store floors and the upper floors, less taxes, property expenses, and replacement provisions. Economic value, based upon stabilized store and floor rental values, is important in indicating the value of the real estate collateral for use other than as a department store. It is important to determine if the ground-floor rent, based upon average store rentals in the neighborhood, can pay carrying charges on the property, taxes, and maintenance and repairs. The upper floors in the average department store have small rental value for other purposes, due to such stores being of a special type of design; hence one has to rely upon the ground floor carrying the load until other use can be found for the property as a whole in the event that the need for such a change in the use of the property occurs.

An important factor in the appraisal of a department store is an analysis of the gross sales and the character of such sales over a period of years. Whether the business is cash or credit must be taken into consideration. Customers patronizing department stores are predominantly women, who deliberate and compare before actually purchasing; only when they are satisfied with the price and quality of the merchandise do they make the purchase. An analysis of gross sales will reveal which departments are thriving and which are lagging.

The gross sales analysis is tied in with the location and area data. What is the population of the area served? What kind of people live in it? Has the population grown? If so, how much? Or has the population declined? How large is the area? What is its pay roll and the volume of business?

The life insurance companies' records of industrial debits and ordinary life-insurance premiums can often give valuable clues of the reasonable future of the subject property's earnings. This investigation would be helpful in the problem of a department store in a small town or metropolitan business subcenter which draws from a localized area. Where the industrial debits of life insurance companies have shown a decline recently, indicating a curtailment of the wage earners' income and consequent buying power, the appraiser should use caution.

Department-store sites are usually large in extent and often are in more than one ownership. In many cases it may be found that part of the site constitutes a leasehold. The appraisal of the value of such leaseholds and of the fee itself in the case where the store may desire to purchase offers many interesting problems.

VALUATION APPROACH

Where the site is owned in fee, the valuation approach should be:

1. LAND: Valuation of entire tract based upon comparison of front-foot values, with due regard to the factor of assemblage.
2. BUILDING: Reproduction cost, less allowance for depreciation and obsolescence.
3. PROPERTY:
    - A. Economic value based upon front-foot commercial rental values for the ground floor and rental value of upper floor space. Generally speaking, a capitalization rate should be used that applies to retail commercial holdings in the district; but some variations are possible since, in many instances, much of the typical department-store space might be classified as warehouse space.
    - B. Economic value based upon the department store's ability to pay rent. The capitalization rate would depend upon what the analysis of the factors previously mentioned in this article revealed, with due regard to the empirical data developed from comparable rental rates within the trade itself.

If part of the property is leased, then the valuation approach should be as follows:

1. LAND: Worth of entire tract, both fee and leasehold.
    - A. Leased portion treated as if owned and the entire property valued upon the basis of a comparison of front-foot values, again with such consideration to assemblage as justified by the circumstances, including the remaining control under the terms of the lease.
    - B. Value of leased portion deducted at its worth as an independent holding adjusted upward or downward in accordance with the benefit or liability reflected in the lease rental paid.
2. BUILDING:
    - A. Reproduction cost, less allowances for depreciation and obsolescence.

  - B. Value of leased portion deducted estimated upon the basis of the injury to the fee if lost, checked against its worth as a part of the leased land if segregated.

3. PROPERTY:
   - A. Economic value based upon commercial front-foot rentals for stores and rental value of upper floors as before.
   - B. Economic value of leased portion by this method deducted in case such portion should be lost.
   - C. Economic value based upon store's ability to pay rent.
   - D. Value by this method deducted in case leased portion should be lost.
   - E. Value of property in fee and value of leasehold, analyzed both upon basis of front-foot store values and rental value of upper floors and also upon store's ability to pay rent for property.

In general, it may be safely said that values for lending purposes can in the majority of instances be best measured where the property is held in fee by the store's rent-paying capacity, provided, of course, that the factor used in the capitalization rate is sufficiently high to compensate for risks inherent in large-scale merchandising operations. In cases where leasehold security is involved the value for mortgage-loan purposes finds its upper limit in an analysis of both front-foot store values and rental value of upper floors as well as upon the store's ability to pay rent for property.

WHAT RENT CAN DEPARTMENT STORES PAY?

It is the belief of the writer that the average well-located, well-designed, and efficient modern department store can at this time pay as rental a rate that will approximate 4 per cent of gross sales.

Information believed to be reliable indicates that stores of the Sears-Roebuck type can pay about 3 per cent of gross business in secondary locations; therefore, it is reasonable to assume that the modern department store in a preferred location should be able to pay 4 per cent as a reasonable rent.

Ordinarily 75 to 90 per cent of the average modern department-store business consists of wearing apparel and kindred lines. If over 25 per cent of the business is in home furnishings, then statistics indicate that such stores can and should pay a higher percentage for rent.

If the business is upon a strictly cash basis, then it will be found that such stores cannot pay as high a rent as stores that do a credit business. Cash-basis department stores operate on a smaller markup, and their selling is largely done on a price-appeal principle.

Many department stores have concession rentals in that they subrent space to tenants offering various specialty lines of merchandise. In such cases research must be made as to what percentage such concessions can pay. Drugs, cigars, groceries, jewelry, sporting goods, hosiery, liquors, men's hats, millinery, shoes, candy, etc. all have different merchandising problems and hence have varying percentages of gross that they can afford to pay for the space occupied.

The modern department store, as a rule, provides the highest and best use for the land on which it is located. The business is primarily the selling of merchandise, and once the shopper enters the store, all space—front, rear, and sides—has more or less equal value for display purposes. The front windows are valuable for advertising-display purposes, and, as the usual area may cover an entire block, the rear of the interior of the store on the various floors is thus as valuable for display of products as any other portions. Usually no courts nor side light is necessary in the design of the building. The feature of high adequacy of use should, therefore, be given major consideration in the appraisal approach.

The pattern of merchandise arrangement should be studied and attention given to space used by the various departments. Usually convenience merchandise and fast-moving inventory items will be found on the parts of lower floors most accessible to the customer. The square footage of selling space should be determined by departments, and it is even possible in this way to check closely probable ground-floor rent and land value for other use. It is also possible, if sales are departmentalized, to determine accurately the rent-paying ability or the amount available for service of the realty by determining the gross operating profit by departments or by capacity of floor space. This again provides a reasonably accurate check on values established by other considerations.

The valuation of department stores brings many interesting problems to the appraiser. This brief outline is intended to cover the primary data that should be assembled and analyzed before the appraiser can feel well enough acquainted with the subject property to be able to assign a value that can be reasonably supported.

VALUES*

WILLIAM DEXTER CURTIS

"What is aught but as 'tis valued?"—Shakespeare

WEALTH represents things of value—character, health, education, real and personal property.

No two persons use the same scales in evaluating their possessions. Because of some intimate association a sentimental value may attach that has little relation to actual worth.

There are false and true values. We are often fooled about the worth of an article we purchase and frequently fool ourselves by false estimates.

It is most important to establish—TRUE VALUES. A person should know with reasonable accuracy what the things he possesses are worth.

Reappraisals from time to time are desirable, for values change. A piece of real property or a merchandise inventory may be worth more or less this year than it was last.

In estimating present worth there are certain facts to be taken into account: such as use, marketability, and obsolescence.

Among various types of value are: market value; replacement value; sound value; loan value; insurance value; tax values; book value; going concern value; liquidating and other values that have become generally recognized.

What a thing will sell for or what it will rent for often determines its value.

The price of an article is its worth estimated in money. Worth is the value estimated in commodities.

Property values are best established by recognized public valuers. The art of appraising has become a highly technical profession, entailing years of careful training and practical experience. The very nature of the work demands a high integrity as well as analytical ability.

Estimates made by reliable, qualified public appraisers are not merely the opinions of some one or more individuals, but recorded knowledge backed by provable facts.

Only duly accredited public appraisers are prepared to defend in court, if need be, their findings. In all cases of this sort judges accept only those persons fully qualified to give expert testimony.

The services of public appraisers are required in the case of—the goods and estate of a deceased person; where one is borrowing on either real or personal property; establishing insurance values and for the purpose of being able to quickly and satisfactorily furnish insurance adjusters definite and complete proof of any fire loss.

There is hardly a person today but what recognizes the value and necessity of fire insurance; the almost equal need for appraisals in matters of this sort is all too often overlooked or considered unimportant.

A manufacturer may have his machinery and plant properly appraised and thus be able to furnish without embarrassment positive proof of any fire loss (as required by all insurance companies) but neglect taking this same precaution with his own home and furnishings.

In addition to knowing the true value of one's material things, it is well to evaluate from time to time one's self. A man should not be averse to taking inventory of himself and appraising those human qualities that either make or mar his character and affect his prosperity.

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The Appraisal Docket

Cases, decisions, and other matters involving rulings and precedents affecting real estate and valuation

William Wilson, Editor

John C. Butler, Assistant Editor

EXCELSIOR!

WE ARE indeed pleased beyond measure at this writing. Our hope that our readers would assist us by furnishing us with references, questions, suggestions, and contributions, to be digested in these columns, has been fulfilled on the grand scale. We take this opportunity to express our appreciation for these matters. We think that they undoubtedly are of interest to the entire appraisal profession.

NEGLIGENT APPRAISALS AND LEGAL LIABILITY

FROM Philip W. Kniskern, M.A.I., of Philadelphia, Pennsylvania, comes reference to the English case of *Baxter* v. *Gapp & Co.* [1938] 4 All E. R. 457 (King's Bench), which involved an action for damages for breach of contract by a mortgagee against an appraiser for negligence in the valuation of property, in reliance upon which valuation the mortgagee was induced to lend money to his subsequent loss. There was no suggestion, and the court so found, that the appraiser acted otherwise than in good faith. The appraisal was found to have been negligently made and recovery was permitted.

The interesting facet of this case is that an opinion—not a statement of fact, mind you—was held upon the facts to have been negligently formed. In the abstract this presents no particular novelty; but as a practical matter it is extremely engaging. We have found no counterpart in the American decisions.

The facts of the case are that the appraiser, who was paid for his work by the mortgagee (this matter of contractual employment is important, as will be noted later), by written report[1] placed a valuation of £1,800 upon a bungalow property in Maidenhead and advised a loan of £1,200 thereon. In reliance upon this, a loan of this amount, secured by first mortgage, was made; subsequently, a loan of £150, secured by second mortgage, was further given. These mortgages were defaulted from the outset; the mortgagee took over possession of the property and bent his efforts toward the realization of the security. The property was finally sold several years later for £850. Damages were recovered for loss of interest, costs of sale, insurance premiums, and loss of principal.

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[1] The report was as follows:

"We have carefully considered the market value of this property, and having taken all matters into consideration, we value this freehold property known as Garden Lodge, Derek Road, Maidenhead, Berks, when the alterations have been completed, in the sum of £1,800, assuming, of course, the property is free from land tax and tithe, and we are therefore prepared to advise, having regard to the Trustee Act, 1925, that the sum of £1,200 be advanced on first mortgage, subject to the amount of £200 being retained until the alterations and additions as above mentioned are completed and passed by us, and we consider this property a reliable trustee security for an advance of this figure.

"*Recommendation* — We advise a re-valuation in, say, five years from this date, in case there should be fluctuations in value due to circumstances we cannot at present foresee."

The court, in its determination of negligence, laid great stress upon the fact that the appraiser was not acquainted with real estate values of Maidenhead properties. The abstract of title disclosed that the mortgagor had paid but £600 for the property. It had changed hands three times in recent years, the top price being £800 or £850. This was discovered after the valuation opinion had been given; nevertheless, it was unchanged. Excerpts from the opinion are absorbing:

> " . . . I do not think that he had very much knowledge of Maidenhead property as such, but he undertook the valuation, and, therefore, of course, in undertaking it he undertook it subject to all the liabilities to which that employment subjected him. I think one may state quite simply the duty which he owed. His duty was, first of all, to use reasonable care in coming to the valuation which he was employed to make and he must be taken to have held himself out as possessing the experience and skill required to value the particular property. If he did not know enough about the property market, or the value of the property at the place where the property was situate, he ought to have taken steps to inform himself of the values of property there, or of any circumstances which might affect the property. It would be no defence, for instance, to say: 'I made this valuation, but the reason why my valuation has proved incorrect, if it has proved incorrect, is that I was not a person, as you knew, who practised in that locality.' . . . . " (Page 459)
>
> "I do not want to say anything more about that, but that is not, to my mind, the difficulty in the way of Mr. Gapp in this case. The question of valuation must to a great extent be a matter of opinion, and must depend on a valuer's experience, but it is difficult to believe that a careful valuer in making a valuation does not endeavor to get some data on which to work. It is not very helpful, especially if a valuation is afterwards challenged to say: 'The only thing that I did was to go and look at the place.' There are questions which can be asked, none of which Mr. Gapp did ask—for instance, what the person has paid for the property." (Page 462)
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> " . . . . One difficulty in the way of Mr. Gapp is that, when his valuation is attacked, as it has been attacked, and when it is said, and said with a great deal of force, that the facts show that this valuation was wholly excessive, the only thing that he can point to as having been done by him to check or support his opinion that £1,800 was the proper valuation of this house was that he cubed it, and, having found the number of cubic feet, took the figure of 1s. 6d. However, that does not help at all, because the proper figure per cubic foot to take is again a matter merely of opinion, and, of course, you can support any valuation if, having got the number of cubic feet, you take the appropriate price per cubic foot. That does not help in the smallest degree, and, reluctant as I am to find that any professional man has not exercised due care in making a valuation, I am forced to the conclusion in this case that £1,800 was an entirely unwarranted sum to put upon this house. . . . . " (Page 464)
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> " . . . . Mr. Vick argued, and put forward with considerable vigour, the proposition that I ought to find here that Mr. Baxter did not rely upon Mr. Gapp's valuation. Where a plaintiff has employed and paid a person to value property for him, and has then advanced the amount of money which the valuer has advised, it requires a good deal to induce a court to say that the client did not rely upon the valuer's valuation." (Page 464)

The decision is correct upon legal principles. It is unique as a practical matter, for it is most difficult to prove that the formation of an opinion—a process more subjective than not—was negligent. Opinions may be wrong, and often are, but that they were wrongly formed (in the absence of fraud or deliberate intention) is quite a horse of a different color.

We commend the opinion. With the growth in dignity and learning of the appraisal profession and the correlative increase in its responsibilities to clientele and public, we shall expect to find similar decisions in this country.

As a matter of law (disregarding the practical difficulty of proof), the legal responsibility of an appraiser to make a correct appraisal can extend even beyond the contractual duty owed to the client. Third parties, of whose existence the appraiser may be unaware, may be induced by reason of an appraisal to change their position to their detriment. The law, assuming the appraisal was negligently made for use beyond that of the client's (that is, intended for public consumption), would afford legal redress to such third parties. The action would not be as for breach of contract (for no contractual relation would subsist between the parties) but would be an actionable civil wrong. This principle has been recognized by statute in the instance of the issue and sale of securities[2] and has found expression, in a comparable profession (that of accountancy), in the common law of this country. *State Street Trust Co.* v. *Ernst,* 278 N.Y. 104, 15 N.E. 2d 416 (1938). That was an action brought by State Street Trust Co. against a firm of accountants for damages suffered by it in reliance upon a certified balance sheet made for Pelz-Greenstein Company by the defendants and by such company submitted to plaintiff in connection with a desired loan. The court found, upon the testimony of expert witnesses versed in proper accountancy, that the certified balance sheet was prepared in grossly negligent form and that it did not represent the true financial condition of Pelz-Greenstein Company, the proposed borrower from the plaintiff. Plaintiff suffered loss by the ensuing insolvency and bankruptcy of its borrower. The action was held to lie. Note that in this case no contractual relationship existed between the accountants and the lending bank. This suit was not therefore for breach of contract but was rather *ex delicto,* for a civil wrong. It is relevant to state the opinion discloses the fact that the defendants knew that Pelz-Greenstein Company was seeking a line of credit from the plaintiff and knew of the contemplated submission of the balance sheet to plaintiff. However, even this element was absent in the case of *National Surety Corporation* v. *Lybrand,* 256 App. Div. 226, 9 N.Y.S. 2d 554 (1939) which involved a suit by a surety on a fidelity bond (issued upon a defalcating employee of a brokerage firm) against accountants to recover for their failure to discover and report substantial cash shortages after audit and examination of the books of the brokerage firm. The action was held to lie.

In so far as legal principles are concerned, there is no distinction to be made between accountants and appraisers with reference to their legal responsibility in matters of this kind. The professional analogy is not only appropriate, it is pertinent.

VALUATION OF FRACTIONAL INTERESTS IN REAL ESTATE

HENRY S. RAAB, M.A.I., of Richmond, Virginia, submits the question whether for purposes of estate or inheritance taxation the legal decisions recognize the diminution in value (over and above the mathematically proportionate share) which real estate undergoes by reason of fractional ownership. An examination of the authorities on this point discloses that such diminution is sanctioned by the courts and administrative boards provided preponderant testimony has been given with reference to the particular realty involved as to the existence of diminution, if any, and its extent. *William R. Stewart, Jr., et al. as Ex-*

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[2] The Federal Securities Act of 1933, with reference to civil liabilities on account of false registration statement, provides by § 11 (a) as follows:

> "In case any part of the registration statement, when such part became effective, contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading, any person acquiring such security (unless it is proved that at the time of such acquisition he knew of such untruth or omission) may, either at law or in equity, in any court of competent jurisdiction, sue—
>
> (4) every accountant, engineer, or appraiser, or any person whose profession gives authority to a statement made by him, who has with his consent been named as having prepared or certified any part of the registration statement, or as having prepared or certified any report or valuation which is used in connection with the registration statement, with respect to the statement in such registration statement, report or valuation, which purports to have been prepared or certified by him; . . . ."

ecutors, etc. v. *Commissioner of Internal Revenue,* 31 B.T.A. 201 (1934) (estate tax). The earlier decisions of the Board of Tax Appeals which purport not to permit diminution beyond the aliquot portion of the fraction to the whole may be explained on the grounds (1) that the board does not take judicial notice of such diminution (as had the transfer tax authorities of the state of New York) and (2) that no evidence was introduced as to the fact and extent of such diminution. *Appeal of Clifford A. Cook, Executor of the Will of Charles A. Claflin,* 2 B.T.A. 126 (1925); *Appeal of the National City Bank of New York, et al., Executors of the Estate of Julian H. Barclay, Deceased,* 2 B.T.A. 696 (1925); *Adelaide McColgan, Administratrix c.t.a., etc.* v. *Commissioner of Internal Revenue,* 10 B.T.A. 958 (1928). In the *Stewart* case, *supra,* a discount (over and above the aliquot portion) of 15 per cent of the mathematical equivalent of the value of the entire parcel was granted upon testimony, the court's resumé of which is as follows:

> "In support of their contention that fractional undivided interests in real estate in New York have not a value equal to a like fraction of the fair value of the entire parcel the petitioners have offered the testimony of two qualified experts in New York real estate. One of these testified that in his experience it was hard to find a buyer for minority fractional undivided interests in real estate in New York City. He testified that ordinarily fractional interests were sold in connection with other fractional interests; in other words, that a purchaser of property was not interested in purchasing fractional interests, but that where he was interested in purchasing a parcel of real estate and could purchase several undivided interests making up the total he would make the purchase; and that where the owner of a fractional interest tried to sell it, he found he could not secure a purchaser except at a substantial discount. Another of the petitioners' witnesses testified that he and his firm had made a number of sales of fractional interests in real estate over a period of more than 20 years and that in practically every case a purchaser could be found for the fractional interest only at a discount. He cited one particular case where a person desiring to purchase a given piece of property was willing to pay $55,000 for the total parcel but would pay and did pay only $16,000 for a one-third undivided interest. He further testified that the owner of an undivided interest of a parcel of real estate is limited in the control, management, operating, and renting of the building; that he is limited by the wishes and whims of the other co-owners; that it is a consideration of these factors that makes it very difficult to find a purchaser for minority fractional interests. He admitted that under the New York law the owner of an undivided interest could bring a partition proceeding for the sale of the property, but testified that some such proceedings were long drawn out and that often a prospective purchaser for the entire property was not interested in acquiring the property after the partition proceedings had been completed." (Page 204)

As stated above, the transfer tax authorities of the state of New York have in the past permitted what might for convenience's sake be termed an "excess diminution" of at least 10 per cent in the valuation of undivided fractional interests in New York real estate. This procedure has found judicial sanction in the courts of that state. *In re Gibert's Estate,* 176 App. Div. 850, 163 N.Y.S. 974 (1917) (an "excess diminution" of 15 per cent was there found proper). The rationale of this practice is explained as follows:

> "It is conceded that it is proper to make a deduction in valuing an undivided fractional interest in real property because of the diminution of value which results from the fact that it is an undivided fractional interest only. This deduction is due in part to cover the expenses incident to a partition action, but is chiefly due to the fact that the owner of such an undivided interest, particularly if, as in the case at bar, it be a minority interest only, cannot control it, but holds it practically at the mercy of the owners of the other interests. For such an interest there is only a limited market, the proof being that experience shows that the purchasers of undivided interests are usually speculators and operators. This restrictive market for such interests lowers their market value." (Page 974)

An analogous application of this principle was made in the valuation of split or participation shares or certificates in mortgages. *In re New York Title and Mortgage Company,* 277 N.Y. 66, 13 N.E. 2d 41 (1938) (allowance of an "excess diminution" of 15 per cent).

RETROSPECTIVE VALUATIONS OF CEMETERY PROPERTIES

LEST those of our readers whose patience or curiosity have carried their perusal this far doubt that we have lost our professed matinal jubilance and now treat with such somber matters as suit our mood, we rush to reassure them that, paradoxical as it may seem, we write of a living subject which spasmodically—as if by reflex action—appears in the legal decisions. We refer to the recent case of *Montrose Cemetery Co.* v. *Commissioner of Internal Revenue,* 105 F. 2d 238 (C.C.A. 7th, 1939). We think this case will be of interest to Martin W. Lederer, of Milwaukee, Wisconsin, to whose able articles, "The Appraisal of Cemeteries" (*The Appraisal Journal,* Vol. V., Nos. 2 and 3) we commend our readers.

In the determination, for Federal income tax purposes, of the gain or loss resultant from the sale or other disposition of property (made after March 1, 1913, but acquired before such date), the taxpayer is given the alternative of selecting cost or fair market value as of March 1, 1913, as his basis. Revenue Act of 1938, § 113a (14). As, in many instances, "fair market value" is greater than "cost," the former is the more economical choice for the taxpayer. Such choice, however, necessitates the preparation of a retrospective appraisal as of March 1, 1913. This presents quite a practical problem, nor are the difficulties alleviated by interment. Exhumation is now and then required.

The fountainhead of authority in matters of Federal income taxation is lodged in the Supreme Court of the United States. We shall thereto ascend and proceed downstream. The case of *Elmhurst Cemetery Co.* v. *Commissioner of Internal Revenue,* 300 U.S. 37 (1937) presents the following set of facts: Petitioner in 1909 purchased 137 acres of land near Joliet, Illinois, for $60,000. Thirty-seven acres were divided into plots and developed for cemetery purposes at a cost of $35,000. Some 36,000 square feet were disposed of during the years 1909 to 1913 at prices ranging from 70.2 cents to 79.5 cents, the average for the year ending March 1, 1913, being 76.6 cents. In the three years 1926, 1927, and 1928, 42,000 square feet were sold at a price range of $1.55 to $1.77. In the establishment of the fair market value as of March 1, 1913, of such 42,000 square feet, the Commissioner contended for a value of 23.96 cents—one which took into consideration the then present value of a future sale, or, in other words, a discounted sales value. The Board of Tax Appeals approved the petitioner's contention that the fair market value of the 42,000 square feet is best ascertained as of March 1, 1913, by reference to the analogous sales effected at such time at an average of 76.6 cents per square foot. The Commissioner's contention was upheld by the Circuit Court of Appeals, but was reversed by the Supreme Court, which upheld the Board's determination of value.

The next ebullience of the problem is presented in the case of *Fairmont Cemetery Association* v. *Commissioner of Internal Revenue,* 67 App. D.C. 345, 92 F. 2d 496 (1937). This case, treated in the second of Mr. Lederer's articles (and see *The Appraisal Journal,* Vol. V, No. 3, page 251) involved the retrospective appraisal of a portion of a cemetery unimproved as of March 1, 1913, and improved and sold during 1927 to 1930, inclusive. The Board of Tax Appeals reached the conclusion that this land could be assigned values of 15, 9, 6, and 3.968 cents per square foot (depending upon location) as of the determinative date (March 1, 1913). Such valuation was disapproved on the appeal to the Circuit Court as being too low, the court pointing out that the agreed value of the improved land as of March 1, 1913, was 80 cents per square foot and that the average cost of improvement was but 10 cents a square foot. Denmark's much maligned fragrance was detected by the court. The decision was important in that it held: (1) evidence as to the value of near-by farm lands was excluded as not pertinent to the value of the unimproved cemetery property (as Mr. Lederer says, this decision in effect concludes that the unimproved acreage may be reasonably considered as a part of the entire enterprise); (2) the valuation as of the determinative date of cemetery lands, whether improved or unimproved, is best shown by comparison with the contemporaneous selling prices of lots; and (3) the discounted sales-value theory was not countenanced. The same conclusions were reached in *West View Cemetery Association* v. *Commissioner of Internal Revenue*, 95 F. 2d 714 (C.C.A. 5th, 1938). In that case, however, Mr. Justice Sibley dissented, saying on these points:

> "If the majority opinion means, as I think it does, that the Board must value all land in the improved area at what just previously some like land had sold for without any reduction for probable delay in sale, I earnestly dissent. That idea would obtain for goods or land for which there is a general market, but not for superabundant cemetery lots the demand for which is limited by deaths and prospective deaths in the community. They cannot be used for any other purpose, and when the present demand is satisfied the seller must wait.
>
> "The fair market value as of March 1, 1913, for which we are searching is the statutory substitute for the usual cost basis in determining gain on a sale. If this taxpayer had bought the cemetery on March 1, 1913, a proportional part of what was then paid would be the cost basis for the lots sold in 1930 and 1931. The fair market value for which we are inquiring since there was no purchase then, is what the taxpayer or another would reasonably have paid if there had been a purchase on that date. It is very manifest to me that no purchaser would have bought even the improved area at the price per square foot at which some lots from it were retailed. He would know that one must wait many years for a return of his money, and would therefore offer much less. The Board has only attempted to do what any purchaser would have done in figuring on a purchase of this property as cemetery lots in 1913. There is nothing unlawful or unreasonable in it, and by consequence nothing that this court can reverse." (Page 718)

Certainly the comments of Mr. Justice Sibley have the concurrence of all economists and appraisers. In the last analysis, the value to be computed is the fair market value as of March 1, 1913, of property subsequently sold—the value which would result from the negotiations of the theoretically ubiquitous willing seller and buyer. Since our buyer is no single-lot purchaser and since the demand for cemetery lots is at any one point of time quite limited, it is apparent that the negotiations would reflect (and discount for) the estimated sales life of the entire cemetery. It thus becomes immaterial whether we compute value in bulk (as for the entire cemetery) or piecemeal (as for individual lots and graves). It was upon this point that the majority went astray in the *West View Cemetery* case, *supra*, when it said that: "What was in question here was not the market value of the cemetery lots as a whole in 1913, but the market value of the sold cemetery lots, as lots in that year, if they had been put up for sale and sold at the fair market price then obtaining." (Page 716)

However this may be, the result of the decision in the *Montrose Cemetery Co.* case, *supra*, is to render all discussion of the point quite moot. That opinion refused to conclude that the *Elmhurst Cemetery Co.* case (300 U.S. 37) prescribed an exclusive method of valuation: viz., retail sales of lots sold during the basic year of 1913. Instead, it formulates what may for convenience be dubbed as the "substantial evidence test": *viz.*, one which weighs all the elements bearing upon fair market value (including the discounted-sales or present-value method, the use of which as an indicative though not conclusive test of value was approved). The point at issue in the case was the fair market value as of March 1, 1913, of 14,993.67 square feet of cemetery property sold in 1931. (No single lot purchase here!) The record disclosed, by the petitioner's own witness, that the cost of the raw land was 2.75 cents per square foot, and that the cost of the entire improvement and maintenance for the cemetery was 25 cents per square foot. The Commissioner fixed the determinative value as of 21.5 cents; the Board, at 23 cents per square foot. Yet petitioner, relying upon values obtained for individual purchases during the basic year, claimed a value of 94 cents. The court noted the following facts: (1) The 1913 income of the cemetery was $31,902.48. Capitalizing an income of $30,000 at 5 per cent, a present valuation of $600,000, based upon prospective net earnings, is reached. Such valuation was equivalent to a square foot value of about 27 cents. (2) In 1920, petitioner had three retrospective appraisals made as of 1913, each of which fixed a value of 15 and 25 cents per square foot for unimproved and improved land respectively. These values were used for tax purposes by petitioner. (3) Petitioner's capital-stock tax returns showed a value below 20 cents. (4) The conversion cost of the raw land (2.75 cents) to improved property (at 25 cents cost) would not square with petitioner's claim for 94 cents.

It is interesting to note the method by which the Commissioner reached his valuation of 21.5 cents:

> "The Commissioner, Richards, and Lockwood valued the unsold lots and graves in 1913 on the present-value method using Hoskold's formula with interest rate at 4 per cent and risk rate at 8 per cent. In accord with the present-value method, the average selling price to be received for the unsold land (based on the retail prices of the sold land) and the time required to sell the unsold land are first anticipated. The unsold land multiplied by the average price per square foot then gives the total expected amount to be received for the unsold land over the period of time in question (the expected life of the cemetery). This unrealized amount is then discounted to present value by the use of Hoskold's formula. In addition, Lockwood also applied the reproductive appraisal method or the cost of reproducing the cemetery as it was on March 1, 1913." (Page 242)

The Board of Tax Appeals (and what puissant pussyfooting was there!) criticized this method, stating that the use of the present-value method (in this case, 21.5 cents), or the use of the retail sales (in this case, 94 cents), alone, was not justified. It considered all the evidence and arrived at a value of 23 cents! Parenthetically speaking, we reluctantly observe that such puissant pussyfooting—a sort of legal embodiment of Uriah Heap— is quite characteristic of the time and of the tempers of our public servants. We much prefer the course sailed by the Commissioner. However, the Board's stratagem carried; its conclusion was upheld by the Circuit Court, which said:

> "Retail sales constitute only one element to be taken into consideration in the determination of the fair market value of the cemetery land, and the use of the retail price method alone is not justified. The same consideration is applicable to the element of time required to sell the cemetery land and the present-value method which is based thereon. Along with the time element and the retail selling price there should be taken into consideration the cost of acquisition of the cemetery, the location, age, size and topography, the state of development, the existence of competing cemeteries, the type of clientele, the trend of population served, annual net earnings, and other related matters." (Page 244)

CEMETERIES SECUNDUM

WHILST we were in the process of exhumation of the cemetery cases, another arm of the subject came to light. An interesting question is posed by the attempt of government to condemn land used for a public cemetery so as to devote it to another and different public use. In *Clarendon County* v. *Holloday*, 182 S.C. 510, 189 S.E. 885, 109 A.L.R. 1496 (1937), certain cemetery property was desired by county authorities for highway purposes; to obtain it, condemnation proceedings were instituted. The court held that since the county proceeded under a general power of condemnation, which power neither expressly nor by necessary implication provided for the disturbance of cemeteries, the suit must fail. The gist of the case was that although cemeteries are subject to the power of eminent domain, the statute with reference thereto must authorize the taking either by express reference or necessary implication; that property devoted to one public use cannot be taken for another, and inconsistent, public use without specific legislative authorization. The same question was posed in the case of *United States* v. *Sixty Acres, More or Less of Land in Williamson County, Ill.*, 28 F. Supp. 368 (D.C., E.D. Ill., 1939). Such was a condemnation proceeding for the much publicized Crab Orchard Creek Project, a Federal public works enterprise of benign design whose practicality rests with history. The undertaking involved the construction of a dam to impound the waters of Crab Orchard Creek (a non-navigable stream) into a lake several miles in area, which action would inundate the lands here in question, being lands used for public cemeteries. The court there overruled the contention of the defendant landowners, holding that: "While it is a well-recognized rule that land devoted to a public use may not be taken for another inconsistent public use under the power of eminent domain unless the intention of the legislature to that effect has been manifested in express terms or by necessary implication, this rule is ordinarily applied in grants of power to public service corporations and not where the power is being exercised by the State itself for its immediate purposes." (Page 372) We submit that this is a distinction without a difference. A public use—theoretically, at least—is being fulfilled, whether undertaken by the government or by a privately owned corporation, whenever condemnation is permitted. The media is unimportant to the instant question. Nevertheless, the distinction sounds well, which is apparently the ultimate in these our times.

UPON THE VALUATION OF PUBLIC UTILITIES

ON March 7, 1898, precedent of far-reaching importance on the subject of public utility valuation was made when the United States Supreme Court handed down its famous decision of *Smyth* v. *Ames,* 169 U.S. 466. That case concerned a constitutional challenge to legislation of Nebraska which undertook to fix maximum railroad rates for intrastate freight traffic. The point at issue was that the maximum rates permitted were insufficient to provide a fair return upon property used and useful in the public service and hence constituted a deprivation of such property without due process of law within the meaning of the Fourteenth Amendment to the Federal Constitution. In the determination of this it naturally became necessary to establish a value of the property so used and useful in the public service. The Supreme Court held that the rates were constitutionally insufficient, remarking in the course of its opinion:

> "We hold, however, that the basis of all calculations as to the reasonableness of rates to be charged by a corporation maintaining a highway under legislative sanction must be the fair value of the property being used by it for the convenience of the public. And in order to ascertain that value, the original cost of construction, the amount expended in permanent improvements, the amount and market value of its bonds and stock, the present as compared with the original cost of construction, the probable earning capacity of the property under particular rates prescribed by statute, and the sum required to meet operating expenses, are all matters for consideration, and are to be given such weight as may be just and right in each case. We do not say that there may not be other matters to be regarded in estimating the value of the property. What the company is entitled to ask is a fair return upon the value of that which it employs for the public convenience. On the other hand, what

> the public is entitled to demand is that no more be exacted from it for the use of a public highway than the services rendered by it are reasonably worth." (Pages 546-47)

This was the opinion which bestowed judicial benediction upon the "fair-value" rule of public utility valuation under which rule the courts, ever since, have insisted that original cost, reproduction cost, commercial value, and various other factors must all be taken into consideration in fixing a utility rate base. It is an opinion railed at by the minions of the so-called "New Deal," whose contentions are that "fair value" is "unsound in principle and unworkable in practice" and should be replaced by the rule of "prudent investment" or "original cost." Particularly obnoxious to the avid advocates of a new (and therefore better!) "streamlined" system of utility rate making is the reproduction-cost method of valuation.

Golden opportunity seemed to present itself to the government in the attempt of the Edison Light and Power Company to set aside a temporary rate cut order of the Pennsylvania Public Utility Commission. The Pennsylvania utility law, modified in 1937, makes provision for a temporary rate "[sufficient to provide a return of not less than five per centum upon the original cost, less accrued depreciation, of the physical property (when first devoted to public use) of such public utility, used and useful in the public service]" pending the determination, often a lengthy affair, of final utility rates. P.L. 1053, Purdon's Pa. Stat. Ann., 1938 Supp., Title 66, §1150. If upon the determination of the final rates, the temporary are found to have been inadequate to the utility, provision is made for recoupment. [§ 1150 (e)[3]] In the appeal of the case to the United States Supreme Court, *Driscoll* v. *Edison Co.,* 307 U.S. 104 (1939), both the Federal Power Commission (F.P.C.) and the Federal Communications Commission (F.C.C.), in co-operation with the Department of Justice (Messrs. Jackson and Arnold, et al.), intervened with the plea that the court was afforded "an opportunity to write off the books an unsound and unworkable rule of rate making." This opportunity was not accepted, although Messrs. Justices Black and Frankfurter, by the latter's concurring opinion, took occasion to deplore the "new vitality needlessly" given "to the mischievous formula for fixing utility rates in *Smyth* v. *Ames,* 169 U.S. 466." The case itself was decided adversely to the public utility, since the court held that the commission, in the establishment of the temporary rates, did not confine itself to the single factor of original cost less depreciation, but interpreted the statute as requiring that weight be given also to reproduction cost, going-concern value, and the necessity for working capital. The court did remark that the single factor establishment "would raise the novel and important question of the constitutionality of a temporary rate, based solely on depreciated original cost, with provision for recoupment of the loss from insufficient temporary rates." (Page 114)

This latter question was raised in the case of *Beaver Valley Water Co.* v. *Dris-*

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[3] (e) Temporary rates so fixed, determined, and prescribed under this section shall be effective until the final determination of the rate proceeding, unless terminated sooner by the commission. In every proceeding in which temporary rates are fixed, determined, and prescribed under this section, the commission shall consider the effect of such rates in fixing, determining, and prescribing rates to be thereafter demanded or received by such public utility on final determination of the rate proceeding. If, upon final disposition of the issues involved in such proceeding, the rates as finally determined, are in excess of the rates prescribed in such temporary order, then such public utility shall be permitted to amortize and recover, by means of a temporary increase over and above the rates finally determined, such sum as shall represent the difference between the gross income obtained from the rates prescribed in such temporary order and the gross income which would have been obtained under the rates finally determined if applied during the period such temporary order was in effect.

coll, 28 F. Supp. —— (D.C. W. Pa., 1939), which held that, in view of the recoupment provision of the statute,[4] the statutorily authorized single factor of depreciated original cost is constitutionally proper. Pertinent is the court's comment that if all the elements promulgated by *Smyth* v. *Ames* are requisite in the consideration of a temporary rate, "the case would be ripe for the fixing of final rates and the necessity for temporary rates would be at an end. It was this very situation which the Pennsylvania Legislature intended to meet when it promulgated a formula for the fixing of temporary rates." 7 *U.S. Law Week,* pages 101 and 102. A statute of New York, similarly providing for such a single-factor establishment of a temporary rate, was construed as making mandatory a recoupment to the utility upon the determination of the final rates, if loss it had suffered, and was therefore considered constitutionally valid. *Bronx Gas and Electric Co.* v. *Maltbie,* 271 N.Y. 364, 3 N.E. 2d 512 (1936).

Notwithstanding the decision in the *Driscoll* v. *Edison Co.* case, *supra,* three members (Messrs. Healy, Eicher, and Frank) of the Securities and Exchange Commission took occasion, in connection with the application of the Central Illinois Electric and Gas Company for exemption of securities under §6 (b) of the Public Utility Holding Company Act of 1935, to blast away at the reproduction-cost method of public utility valuation and to advocate the basis of "sales and exchange value" as the proper criterion for the approval of new securities issues. *In re Central Illinois Electric and Gas Co.,* Holding Company Act Release No. 1592 (June 21, 1939). Commissioner Healy has to say:

> "The present case is not a rate case. The issue is not whether the applicant's property is being confiscated because it is not permitted to make a fair return upon the present value of its property. We are dealing with the recording of property on books of account to balance the issue and sale of securities to the public. I know of nothing in law or accounting that justifies the recording of estimates of reproducing property new on books of account. *Smyth* v. *Ames* does not justify it; first because that case dealt only with rate-making and the confiscation issue, and second because even under that decision an estimate of reproduction cost was only one of several elements to be considered."
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> * * * * *
>
> "The view that *Smyth* v. *Ames* in some way justifies the recording of reproduction estimates on books of account and the issuance of securities of an equivalent amount is based upon a distortion and misapplication of that famous decision and has done incalculable injury both to the public and to the utility industry."

Commissioner Eicher adds:

> "*Smyth* v. *Ames,* unfortunately, as Judge Healy points out, has been perverted to support 'reproduction cost new' as the controlling, if not the exclusive, factor in the determination of the rate base. Under the opinion's plain language there is no justification for applying the reproduction cost yardstick beyond the demonstrated need for present or prospective replacements in existing plant during the probable period of revised rate incidence."
>
> * * * * *
>
> "Still less is there any reason or justice in permitting a periodic reappraisal to bulwark additional securities issues beyond the fair values gauged by the prudent investment upon which privately owned property devoted to public use enjoys constitutional protection against the confiscation that would result from the imposition of rates yielding less than a fair return. Such practice inevitably spawns the serpentine circle of higher rates followed by higher reappraisals to support more securities issues, and vice-versa, ad infinitum."

Commissioner Frank comments in the following vein:

> ". . . . I fully agree that, in considering the issuance of new securities, 'sales or exchange value' is the proper criterion for this Commission. The courts have said that sale or exchange value is to be determined by the reasonably expected future earnings of the property; the courts have so held in condemnation cases, in cases involving purchases by municipalities under contracts, and in reorganization cases. . . . . Accordingly, when we are considering the issuance of new securities, the controlling factor is the reasonable expectation of the future earnings of the issuing company. . . . .
>
> "It follows, then, that the rate base is not the controlling factor in determining the propriety of the issuance of new securities. . . . ."

Reproduction cost new, less depreciation, is in the doghouse.

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[4] *Supra,* n. 3.

What to Read

Comments on recent surveys, books, and articles of interest to real estate appraisers

C. M. Jones, Editor — **Librarian, American Institute of Real Estate Appraisers**

BOOK REVIEWS

Monchow, Helen C. SEVENTY YEARS OF REAL ESTATE SUBDIVIDING IN THE REGION OF CHICAGO. *Evanston, Illinois: Northwestern University, 1939. 193 pp.*

EASILY the most outstanding book ever published on real estate subdividing is Helen C. Monchow's *Seventy Years of Real Estate Subdividing in the Region of Chicago,* written as a Ph.D. thesis and just published as Number 3 in Northwestern University Studies in the Social Sciences. Dr. Monchow, Managing Editor of *The Journal of Land & Public Utility Economics,* is the author of *The Use of Deed Restrictions in Subdivision Development* and many articles in the field of land economics.

A sizable number of magazine articles, both good and bad, have been written by theorists and practical land developers on this subject. A few monographs on specific phases have been published. A few books devote isolated chapters to the subject. But no attempt has ever been made to cover exhaustively the economic implications of subdividing land.

No better laboratory could be picked than the Chicago area—cosmopolitan in industry, business, and population. No better period could be chosen than the seventy years from the Chicago fire in 1871 down to the present time—a period which coincides with the rise of a great metropolis from a population slightly less than 300,000 to very nearly 3,500,000. This span of years, covering as it does five major cycles, is adequate to show distinct trends and definite conclusions.

The book has eight chapters, as follows: "The Subdivision Problem," "Population and Subdividing Activity," "The Need for Subdivided Lots," "The Effect of General Business Conditions on the Market for Subdivision Lots," "The Relation of Manufacturing and Transportation to Subdividing Activity," "Institutions Affecting the Sale and Purchase of Subdivision Lots," "A Recapitulation," and "Control of Subdividing Activity."

Real estate subdividing as it has been carried on in the United States, particularly in the vicinity of large cities, has been characterized by extreme irregularity and great economic waste. What work has been done in the field has ignored, for the most part, the underlying causes of these irregularities which in a large measure account for the economic wastefulness. Current interest in land planning and in costs of land development suggested the desirability of analyzing the causes of these irregularities as one step toward developing a plan for control and the promotion of a more economic development of urban areas in the future.

The primary data of the study consist of the number of lots placed on record annually in the office of the county recorders in the Chicago region, which comprises an area within a fifty-mile radius of the Loop. This large area was broken up into local areas, each dominated by a single urban center. The result was the designation of thirty-six local areas, classified as "independent" and "suburban" according to the degree of their dependence upon Chicago proper. These thirty-six local areas were then studied in the light of certain questions:

1. To what extent was subdividing responsive to population growth? In the independent cities, it was found that a fair degree of correlation exists between population growth and lot increase. The relation, however, could not be interpreted as causal, largely because of the tendency of lot increase to anticipate population growth. The relation was found to be considerably less close in suburban cities.

2. Does subdividing take place in response to the need for urban lots? The need for urban sites was taken to include the number of lots necessary (a) to house the existing population according to the standards of the community; (b) to take care of the normally expected population increase over a two-year period; and (c) to meet the business-site needs of the community at present and for two years in the future. This composite, derived measure of need had to be resorted to in the absence of data on lots actually used for these purposes. Comparison of the number of lots needed with the number of lots recorded showed a large surplus (a large number of vacant lots) in all but four of the thirty-six local areas. Statement of this surplus as a percentage of lots needed and the examination of its trend during the sixty years covered by this study showed a constant tendency for lots to be provided far in excess of need for them, and this tendency was more pronounced in suburban than in independent cities.

Upon the basis of the figures collected, the author hazards a measure of residential lots needed according to population. The ratio of twenty-two residential lots on the average per one hundred of the population is a rough rule of thumb which may be used for preliminary estimates and tests in the preparation of zoning ordinances, city plans, housing surveys, and the approval of subdivision plats. This is the first attempt ever made to arrive at a measure of residential needs. Further studies should be made to test the accuracy of this preliminary figure.

3. Is subdividing activity a function of current business conditions? To answer this question the number of lots recorded annually was compared with the volume of industrial production. In general, the conclusion was that the two series tended to move together, without evidence of a causal relation between them. The trend of subdividing activity was also compared with four other series: land values, volume of building construction, rent levels, and other investment opportunities as represented by stock and bond market activity. Land values, rent levels, and stock market trends seemed to bear some casual relation to subdividing as evidenced by their tendency to lead the upswings of the subdivision cycle. However, construction, purchasing power, credit expansion, and the level of the interest rate tended rather to move with subdividing activity and to condition the market for subdivision operations. No one of these factors alone explains the trend of real estate subdividing, but taken together and along with the trend of general business and with the peculiar atti-

tudes toward land purchase, they constitute a group of factors which cause active subdividing of urban areas.

4. Do periods of industrial expansion and of transportation improvement coincide with periods of active subdividing? A fairly close correlation between both manufacturing and transportation developments and subdividing activity was shown. In independent cities manufacturing seemed to show a closer relation, whereas in suburban communities transportation appeared to exert the stronger influence. For both types of development and in both types of communities a tendency was evident for subdividing to precede actual establishment of a manufacturing plant or actual construction or extension of a transportation line.

5. To what extent has subdividing been stimulated or retarded by changes in the laws and practices relating to land transactions? This is one of the most valuable chapters in the entire study. Here for the first time we have a clear picture of the place of the corporation in real estate development. Syndicates, land associations, and land trusts are also considered. Particularly good is the section dealing with the land contract, with its concise listing of the relative advantages and disadvantages to both buyer and seller. A consideration of the auction method, employing mass psychology to stimulate sales, and a section on options with their potentialities for large profits are included in this chapter.

Step by step this minute analysis of the causes of subdividing activity has established the conclusion that we have been developing our land haphazardly with a tremendous amount of economic waste, thereby creating serious problems of public policy. And what of the future? What can be done to avoid past errors and to promote more economic development of urban areas? The author considers three directions for control. Government ownership is not in line with American institutions. Education in the economics of land investment and land development is dismissed as being too slow to meet the urgency of present needs. Various measures already applied, such as control over quality, quantity, situs, license laws, improvement in the form of the land contract, increased control by lending agencies, and devices for promoting the continued responsibility of the subdivider, are considered in detail. Here the author has done an exceptionally fine job in sketching all attempts made in the past to impose some sort of control over urban land development. Her search into every existing method has been exhaustive, but she wastes no words in assembling factual history. While attempted controls have been spasmodic and erratic, nevertheless they receive the author's approval. Co-ordinated control, however, is recommended instead of the multiplicity of agencies and measures now being employed. Upon the basis of the great stake which the public has in the orderly development of urban areas, public utility status for urban land is urged as the best means of promoting stabilized urban development.

Appraisers must know economic trends and policies. They must be keen students of entire areas. All real estate men must be aware of changing concepts in the field from which they derive their existence. Here is a source book which not only concisely sets forth past history but also ties that experience to the rapidly increasing problems of the present and suggests future concepts and policies worthy of much thought and consideration.

Woods, Ralph L. **AMERICA REBORN: A PLAN FOR DECENTRALIZATION OF INDUSTRY.** *New York: Longmans, Green and Co., 1939. 376 pp., $3.00.*

THE CENTRAL theme of this volume concerns itself with the decentralization of America's cities. Mr. Woods attacks the problem with a verve and gusto which not only makes interesting reading but also gives the lay reader an insight into the magnitude of the difficulties presented by this trend.

The presentation of the subject begins with a historical background, the growth of industry and the city being traced from the year 1890 to 1930. Then comes an analysis of the forces which are causing decentralization to proceed at a continually accelerated pace. Social blight of cities, the costs and waste of concentration, the decline of our economic momentum, and changes in industry are treated consecutively.

The conclusions reached are both novel and interesting. Although the urban centers of the country have grown, like Topsy, without rhyme or reason, Mr. Woods holds that to maintain the foundations for a cultivated life there must be a more just and balanced distribution of social and economic benefits.

This volume, while advocating decentralization, holds that this process must be planned if we are to preserve our heritage as a democratic nation whose standard of living is far above that of the rest of the world.

For those whose business concerns itself with real estate, this book is a great contribution. The data presented are monumental in scope, and the tables, appendices, notes, bibliography, and index add greatly to its value and practical use.

ROBERT H. ARMSTRONG, M.A.I.
New York, New York

Aronovici, Carol. **HOUSING THE MASSES.** *New York: John Wiley & Sons, Inc., 1939. 291 pp., $3.50.*

THERE have been scores of volumes published about housing during recent years, and the majority have been written by individuals of the "single-track" mind variety who have shown little appreciation of the fact that housing constitutes not only a social problem but a business and economic problem as well.

Dr. Aronovici, as one of the nation's foremost housing experts, has written this book from a long-range viewpoint. Although the reader may not always agree with a number of the premises and conclusions, he nevertheless will probably agree that the author has been eminently fair in his presentation of various aspects of the subject matter.

The book is divided roughly into three parts. The first part is given over to a discussion of land values and land policies as they are related to housing, following which there is a short study of the people who make up the market. Then come, successively, chapters entitled "Money" and "Earning Capacity and the Housing Market," which treat with costs and the relationship of various income groups to our present supply of housing.

The second part of the book, less statistical in its nature, gives the author's views on "Home Ownership," "The Law and Housing," and "Urbanism and Architecture." It is interesting to note that Dr. Aronovici leans toward the theories of Stuart Chase relative to the ownership of homes by the middle- and lower-income groups. He holds that, due to the hazards of unemployment in our present capitalistic system, home ownership should not be encouraged among those classes at the present time. Doubtlessly this view will engender little sympathy among realty interests, but even if Dr. Aronovici has overstated his case, there is still enough truth in what he has to say to encourage further thought and study relative to this problem.

The third and last part of the volume deals with "Housing Education" and "Housing Surveys and Research."

To date there have been too little data available concerning the entire field of housing, and here is set forth an excellent outline for such a study. There is not only an index but also a brief discussion of modern housing literature at the end of the book.

All in all, the book is extremely well done and may be listed among the best published to date in its field. It deserves a place on the bookshelf of everyone interested in real estate in all its phases.

ROBERT H. ARMSTRONG, M.A.I.
New York, New York

NEW ARTICLES

THE JOURNAL OF LAND & PUBLIC UTILITY ECONOMICS

"Land Classification to Aid the Appraiser," by Conrad H. Hammar

The author, who is Professor of Agricultural Economics, University of Missouri, discusses the land-classification data now available to the appraiser of farm lands, the usefulness of these data, new developments in the techniques and methodology of land classification, and suggestions for the type of information which a land-classification system should include. Because of longer loan periods on farm mortgages, appraisals must necessarily stand for longer periods. Therefore, the appraiser of today needs more reliable data concerning the effects on land of past and prospective use than he has ever had before. The writer also outlines the more important factors that should be considered in making an appraisal classification: i.e., soils, topography, water, physical hazards, types of farming, yields and production of crops and livestock, location factors, and relevant economic and experiential factors. *(August, 1939, p. 277.)*

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THE JOURNAL OF CERTIFIED PROPERTY MANAGERS

"The Management of Properties Owned by Institutions," by Clement E. Merowit

A prominent New York property manager points out that due to changing economic conditions lending institutions which have taken over vast numbers of properties through foreclosure and have been anticipating a time in the not too distant future when they would be able to dispose of these properties and "relax, with mortgages in their portfolios instead of deeds," may have to remain with their ownership problems for some time to come. The insurance companies, Mr. Merowit points out, are particularly vulnerable to adverse public reaction and in their management policies must give consideration to the building of tenant good will. He proposes a "Public Relations Service," to be supported by a number of institutional owners and management organizations co-operatively. Its aim would be to co-ordinate management policies and to undertake group merchandising and promotion. *(September, 1939, p. 60.)*

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NATIONAL REAL ESTATE JOURNAL

"Planning the Appraisal and Writing the Report," by Nat C. Soule, M.A.I.

That the property itself rather than the appraiser directs what should be done is illustrated in this step-by-step outline of the procedure to be followed in planning the appraisal. One of our M.A.I.s gives his opinion of the logical steps to be considered. "The first thing would be determining the purpose of the valuation; second, the classification of the property; third, the assembling of the data; fourth, the study of the data; fifth, the inspection of the premises; sixth, the computation of the value; and seventh, the writing of the report." Under each of these broad headings the author lists various items which the appraiser must investigate. *(September, 1939, p. 26.)*

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REAL ESTATE RECORD

"National Survey Covers Housing Values"

The National Bureau of Economic Research has just released a report entitled "Differentials in Housing Costs," which contains interesting data for use in appraising. The above report discloses the fact that homes in larger cities are worth over double the value of those in smaller communities. These variations in value are due to "the underlying economic, social and physical differences arising from climate, unequal natural resources, varying degrees of industrial and agricultural development, differences in income, and the extent of urbanization, as well as local customs and traditions." The study also deals with the average rents paid in various regions of the country, relationship between values and rents, and differentials in housing costs. *(September 23, 1939, p. 6.)*

THE REVIEW OF THE SOCIETY OF RESIDENTIAL APPRAISERS

"The Real Estate Situation," by Thurston H. Ross, M.A.I.

This comprehensive discussion of the real estate market in southern California and the weaknesses caused by trying to "create" real estate values is very enlightening. While it deals specifically with the real estate situation in the Los Angeles area, the discussion of the effect that large-scale subsidized housing exerts upon older properties is applicable to all parts of the country. The author stresses the fact that confidence in the real estate men and market comes from satisfying the economic needs of a community with a profit to all. He decries their disregard for the law of supply and demand by oversubdividing, overbuilding, and overselling, thereby glutting the market. He believes that the real estate situation is sound but that more care is needed on the part of the investor. *(September, 1939, p. 5.)*

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SKYSCRAPER MANAGEMENT

"Graphs Show Bondholders How Income Dollar Is Spent," by H. A. Winters

A plan whereby the bondholder may know just where the income dollars in his investment are going is being tried successfully in the Pure Oil Building in Chicago. These graphic presentations not only show the trend of occupancy but also the proportionate percentage of income allocated to each purpose. A comparative graph was also prepared to show the relation of the building occupancy for a five-year period to the general office building occupancy in Chicago. Several of these charts are illustrated. They prove an enlightening source of information concerning the cost of operation for office buildings. *(September, 1939, p. 3.)*

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Robert S. Wayland (506)..........10 State St.
Parker Webb (538)..........24 Milk St.
Richard S. Willis (652)..........87 Milk St.

Brockton
Charles H. McKenney, Jr. (423)..........106 Main St.

Brookline
F. Paul Morgan (735)..........1394 Beacon St.

Fall River
J. Frederick Beckett (167)..........49 Purchase St.
Myer Markell (165)..........56 N. Main St.
Everett N. Slade (53)..........57 N. Main St.

Lowell
John C. Percival (233)..........24 Merrimack St.

Somerville
Harry A. Gilbert (650)..........381 Broadway

Springfield
Henry M. Clark (287)..........100 Broadway
Bion T. Wheeler (339)..........25 Elm St.

Worcester
Francis S. Bailey (524)..........2 Foster St.
F. Everett Cole (556)..........5 Pleasant St.
Charles A. Kabley (501)..........340 Main St.
Maurice F. Reidy (8)..........2 Foster St.

MICHIGAN

Ann Arbor
Louis C. Andrews (653)..........Ann Arbor Tr. Bldg.
Edward M. Couper (654)....204 State Savings Bk. Bldg.

Detroit
Judson Bradway (392)..........533 Majestic Bldg.
Matthew Carey (389)..........2406 Union Guardian Bldg.
George W. Drennan (358)..........617 Penobscot Bldg.
Guy S. Greene (394)..........300 Lafayette Bldg.
Donald D. James (539)..........700 Penobscot Bldg.
Henry N. Johnson (390)..........300 Penobscot Bldg.
W. Gordon Johnstone (700)......1400 United Artists Bldg.
Albert D. MacRae (540)..........Union Guardian Bldg.
Arthur A. May (686)..........950 Nat. Bk. Bldg.
Alfred W. Palmer (312).......1920 Union Guardian Bldg.
Edmund T. Paterson (385)..........3050 E. Grand Blvd.
Leonard P. Reaume (393)..........2150 Buhl Bldg.
George C. Sexauer (395)..........2150 Buhl Bldg.
William W. Tanney (434)..........9061 W. Outer Dr.
Ward S. Van Deusen (665)..........705 Fidelity Bldg.
Clarence S. Vaughn (422).......2103 First Nat. Bk. Bldg.
Carl S. Wells (391)..........2706 Eaton Tower

Flint
Gerald F. Healy (604)..........611 Genesee Bk. Bldg.

Grand Rapids
Isaac R. Blandford (234)........105 Federal Square Bldg.
Leon T. Closterhouse (247)..........Central Bk.
John Garfield Emery (304)..........300 Houseman Bldg.
Harry J. Fuller (235)..........The Michigan Tr. Co.
Peter Hoek (713)..........750 Leonard St., N. W.
Walter S. Palmer (193)..........104 Federal Sq. Bldg.
Arent Van Stensel (248)......701 Peoples Nat. Bk. Bldg.
Charles H. Warden (229).920 Grand Rapids Nat. Bk. Bldg.

Jackson
Henry H. Lammers (557)..........508 Dwight Bldg.

Lansing
Edward G. Hacker (291)........221½ W. Washtenaw St.

Pontiac
Paul A. Kern (134)..........31 Oakland Ave.

MINNESOTA

Duluth
Richard W. Northrup (379)..........600 Torrey Bldg.

Minneapolis
Norman L. Newhall (32)..........519 Marquette Ave.
Edwin L. Somerville (30)......519 Metropolitan Bk. Bldg.
J. Frederick Sutherland (331).......Suite 450, Baker Bldg.

MISSISSIPPI

Jackson
J. O. Manning (299)..........3012 N. State St.

MISSOURI

Clayton
Gunther Meier (319)..........24 N. Meramec Ave.

Joplin
Rolla E. Stephens (264)..........711 Virginia Ave.

Kansas City
George M. Bliss (360)..........17 E. Tenth St.
C. F. Curry (345)..........921 Baltimore Ave.
Ward C. Gifford (667).........709 Nat. Fidelity Life Bldg.
Herbert B. Patt (553)..........417 R. A. Long Bldg.
E. F. Pierson (289)..........311 Commerce Bldg.

St. Louis
W. C. Bernard (91)..........412 City Hall
William W. Butts (93)..........410 Wainwright Bldg.
Herbert O. Byrd (302)..........818 Chestnut St.
Charles J. Daly (94)........211 Old Custom House Bldg., Eighth & Olive Sts.
Chester A. Dougherty (249)..........109 N. Seventh St.
J. Gregory Driscoll (528)..........1501 Locust St.
John H. Farish (201)..........713 Chestnut St.
Grover Godwin (418)..........1796 Arcade Bldg.
Joseph W. Hannauer (15)..........811 Chestnut St.
Alfred B. Kissack (525)..........915 Olive St.
Francis A. Reardon (668)..........111 N. Tenth St.
Monroe H. Rodemyer (218)..........109 N. Eighth St.
Edward M. Thornhill (693)..........807 Chestnut St.
N. S. Wood (131)..........709 Chestnut St.

NEBRASKA

Lincoln
C. C. Kimball (381)..........Stuart Bldg.
W. B. Romans (669)..........2841 Rathbone Rd.

Omaha
Walter T. Greene (742)..........617 W.O.W. Bldg.
Lewis C. Sholes (23)..Care of County Assessor, Court House
Clinton B. Stuht (33)..........Aquila Court Bldg.

NEW JERSEY

Arlington
Edgar H. Bixler (701)..........100 Midland Ave.

Atlantic City
Maurice A. Kelley (325)..........20 S. Tennessee Ave.

Bayonne
George Seymour (670)....................9 W. Eighth St.

Butler
Frank B. Fay, Jr. (171)....................Fayson Lake

Camden
Ralph D. Baker (60)....................924 Broadway
William W. Chalmers (63)....................645 Market St.
Abraham J. Rosenfeld (213)....................300 Broadway
Leon E. Todd (340)....................2623 Westfield Ave.
Philip Zinman (95)....................643 Market St.

East Orange
Frank H. Taylor (6)....................520 Main St.
Harry A. Taylor (108)....................520 Main St.

Elizabeth
John P. Gloeckner (655)....................1143 E. Jersey St.
R. Mason Kirkland (714)....................125 Broad St.
John K. Leeds (99)....................286 N. Broad St.
B. B. Miller (58)....................281 N. Broad St.
James Rosensohn (715)....................125 Broad St.
Max Tieger (112)....................215 Broad St.
Alton W. Van Horn (736)....................215 Broad St.

Jersey City
Percy A. Gaddis (22)....................900 Bergen Ave.
D. E. C. Somers (175)....................700 Bergen Ave.
R. E. Thompson (419)........Centl. R. R. of N. J. Term.

Keansburg
Samuel D. Walker (729)....................1 Church St.

Linden
John Fedor (65)....................540 S. Wood Ave.

Maplewood
Gilbert N. Swett (561)....................Depot Plaza

Newark
Murray Apfelbaum (38)....................17 William St.
George E. Dugan (236)....................18 Washington Pl.
Charles F. Evans (572)....................782 S. 19th St.
Joseph L. Feibleman (66)....................17 Academy St.
George Goldstein (413)....................810 Broad St.
Franklin Hannoch (49)....................14 Park Pl.
Louis Herman (70)....................60 Park Pl.
Charles Frederick Kraemer (366)....................776 Broad St.
Rudolph Kruger (516)....................11 Hill St.
John A. Linnett (85)....................46 Clinton St.
E. J. Maier (75)....................187 Market St.
Joseph L. Pitman (661)....................60 Park Pl.
Joel L. Schlesinger (87)....................31 Clinton St.
Harry J. Stevens (200)....................478 Central Ave.

New Brunswick
James A. O'Connell (186)....................392 George St.

Newton
A. N. Lockwood (433)....................17 Main St.

Ocean City
Elmer Jackson Pearl (330)....................810 Ocean Ave.

Paterson
Joseph R. Lambert (443)....................20-22 Church St.

Perth Amboy
Morris Goldfarb (109)....................265 Madison Ave.

Plainfield
Milton Brown (662)....................131 North Ave.
William G. McDowell (446)....................152 North Ave.

Ridgewood
Frederick A. Tetor (364)............1 E. Ridgewood Ave.
Samuel S. Walstrum (106)..........201 E. Ridgewood Ave.

Rutherford
Charles A. Van Winkle (113)..........1 & 2 Station Sq.
Theodore Van Winkle (117)............1 & 2 Station Sq.

Short Hills
William Clifford, Jr. (716)....................87 Whitney Rd.

NEW MEXICO

Albuquerque
Joseph P. Deasy (377)....................442 Chacoma Pl.

NEW YORK

Buffalo
A. P. Allingham (3)....................158 Pearl St.
P. V. Bowen (141)....................1006 Ellicott Sq.
Walter W. Cohn (81)....................155 Pearl St.
Cuthbert E. Reeves (19)..............Liberty Bank Bldg.

Mechanicville
Franz H. Moak (40)....................37 N. Main St.

Metropolitan City of New York

Borough of Bronx

Herman A. Acker (279)..........318 E. Kingsbridge Rd.
Amedeo Giordano (515)............2488 Grand Concourse
Samuel E. McRickard (292)..........400 E. Fordham Rd.

Borough of Brooklyn

Stephen F. Barrera (133)....................191 Joralemon St.
George Baur (170)....................2609 Clarendon Rd.
Charles D. Behrens (635)....................190 Montague St.
William H. Cary (746)....................146 Montague St.
Joseph William Catharine (503)........149 Pierrepont St.
James P. Clark (550)....................478 Graham Ave.
James B. Fisher (57)....................160 Remsen St.
George H. Gray (17)....................310 Ashland Pl.
Bernard F. Hogan (29)....................451 Fifth Ave.
Arthur J. Horton (183)....................6904 Fourth Ave.
George S. Horton (184)....................59 Lafayette Ave.
Harry M. Lewis (743)....................189 Montague St.
Alfred R. Marcks (718)....................9 DeKalb Ave.
Joseph M. May (744)....................189 Montague St.
Frank M. McCurdy (39)....................44 Court St.
M. C. O'Brien (190)....................798 Nostrand Ave.
Charles Partridge (92)....................397 Flatbush Ave.
Robert E. Patterson (745)....................837 Manhattan Ave.
Lewis H. Pounds (128)....................32 Court St.
Milton T. VanderVeer (660)....................51 Willoughby St.
R. W. Walden (89)....................141 Montague St.
Alfred R. Wittich (649)............99 Pennsylvania Ave.

Borough of Manhattan

Edwin F. Armstrong (702)....................485 Madison Ave.
Robert H. Armstrong (562)....................485 Madison Ave.
Edward J. Crawford (373)....................225 Broadway
Dalton Granger De Witt (315)....................22 W. 48th St.
Sam W. Florence (206)..............2700 Woolworth Bldg.
Howard Geoghegan (512)....................51 Chambers St.
A. N. Gitterman (45)....................45 E. 49th St.
James A. Glynn, Jr. (671)....................100 E. 42nd St.
Bracton Goldstone (68)....................10 E. 40th St.
George Grotz, Jr. (573)....................100 E. 42nd St.
George M. Halk, Jr. (582)....................742 Lexington Ave.
Frank D. Hall (159)....................393 Seventh Ave.
Herbert R. Houghton (703)....................12 E. 41st St.
John R. Hoyt (290)....................17 E. 42nd St.
Robert Huntley (214)....................67 Liberty St.
S. E. Kazdin (269)....................70 Pine St.
Harry K. Keller (563)....................522 Fifth Ave.
John J. McCormick (445)....................51 Chambers St.
Thomas E. McSherry (636)....................51 Chambers St.
Clarence C. Merritt (357)....................50 E. 42nd St.
Charles W. Morrison (270)....................270 Madison Ave.
James R. Murphy (437)....................217 Broadway
Henry Musch, Jr. (157)....................270 Broadway
Charles A. Nehring (521)..........1441 St. Nicholas Ave.
Charles J. Pladwell (542)....................522 Fifth Ave.
Edmund J. Port (688)....................17 E. 42nd St.
George Stanley Potter (656)....................270 Madison Ave.
J. Kingsley Powell (77)....................34 Nassau St.
Andrew B. Rankin (625)....................141 Broadway
Irving I. Rosenbaum (179)....................384 Broadway
Maurice R. Spear (543)....................225 Fifth Ave.
Eldridge C. Thompson (583)....................34 Nassau Street
John C. Tredwell (574)........Rm. 1501, 393 Seventh Ave.
Wallace Whittington True (647)........393 Seventh Ave.
David Vogel (368)....................150 Broadway

Borough of Queens

Armand Brunswick (327)........90-26 161st St., Jamaica
D. Duffy Lane (711)............87-65 52nd Ave., Elmhurst
William F. MacDermott (198)....89-70 162nd St., Jamaica
Axel J. Swenson (272)....41-27 29th St., Long Island City

Nassau County, Long Island

Richard T. Childs (273)............222 Front St., Mineola

Westchester County

Robert A. Anderson (259)....34 E. First St., Mt. Vernon

Vernon N. Bailey (322).........175 Main St., White Plains
Raymond S. DeMott (717).....65 Pondfield Rd., Bronxville
Edward C. Heald (222)...........20 S. Broadway, Yonkers
Edward H. Hufnagel (250)..100 Stevens Ave., Mt. Vernon
Henry F. Linsmann (719)..126 Burkewood Rd., Mt. Vernon
Albert W. Lockyer (294).......Depot Plaza, White Plains
Paul Wegener (90).............144 S. Broadway, Yonkers
Edward M. West (305)......1 Martine Ave., White Plains

Rochester

Warren W. Allen (637)....Lincoln-Alliance Bk. & Tr. Co.
Linus S. Appleby (689)....1014 Lincoln Alliance Bank Bldg.
Abraham Berghash (219)..............130 Clinton Ave., S.

Schenectady

William Garner Bee (415)...................277 State St.

Syracuse

James H. Dawley (333)................121 E. Genesee St.
Edward Eagan (271).........204 Starrett-Syracuse Bldg.

NORTH CAROLINA

Charlotte

S. T. Henderson (20)..........................P. O. Box 965

OHIO

Akron

Charles S. Jenkins (564)..................659 Schiller Ave.
John C. Kyle (102)..................520 S. Firestone Blvd.
E. L. Marting (672).............................27 S. High St.
A. R. Ritzman (544)........................1099 S. Main St.
Eugene K. Sheffield (575).........651 Central Tower Bldg.
Fred E. Smith (298)......608 Broad Blvd., Cuyahoga Falls
W. F. Voges (105)..........................1109 S. Main St.

Canton

Mark Hambleton (146)...................417 Mellett Bldg.
A. Ray Walters (439)....................524 Renkert Bldg.

Cincinnati

Henry B. Bunker (545)......S. E. Cor. Fourth & Vine Sts.
Howard R. Burgess (176)...................304 Neave Bldg.
Fred Droege, Jr. (154)...........410 First Nat. Bk. Bldg.
J. George Ege (335)......................3040 Urwiler Ave.
James W. Farrell (149)......S. W. Cor. Fifth & Main Sts.
James J. Grogan (180)......S. W. Cor. Fifth & Main Sts.
Albert J. Mayer (204)...........1515 First Nat. Bk. Bldg.
P. Lincoln Mitchell (181)....S. W. Cor. Fifth & Main Sts.
Michael J. O'Byrne (429)....3270 Menlo Ave., Hyde Park
Russell Price (152)...........S. W. Cor. Fifth & Main Sts.
Walter S. Schmidt (111)...S. W. Cor. Fifth & Main Sts.
Lewis R. Smith (139)......................409 American Bldg.
John B. Spilker (155)............410 First Nat. Bk. Bldg.

Cleveland

Talmage D. Auble (262)...............15509 Madison Ave.
Robert F. Berwald (300)............1220 Williamson Bldg.
Ben B. Beyer (34)...................1425 Williamson Bldg.
James G. Bingham (328)..........1227 Williamson Bldg.
Raymond T. Cragin (282)..............Nat. City Bk. Bldg.
W. J. Crawford, Jr. (323)..............720 Cuyahoga Bldg.
Walter R. Granger (285)...........310 Hippodrome Bldg.
Joseph J. Haas (164)......................200 Marshall Bldg.
Joseph B. Hall (2)........................5700 Truscon Ave.
Harry D. Knowlton (673).................920 Guardian Bldg.
Laurence H. Lang (694)..................1101 Citizens Bldg.
Joseph Laronge (103)..........600 Union Commerce Bldg.
Edwin H. McIntosh (283)....325 Society for Savings Bldg.
Warren L. Morris (251)............950 Nat. City Bk. Bldg.
C. A. Mullenix (605)............................620 Hickox Bldg.
E. L. Ostendorf (14)...............950 Nat. City. Bk. Bldg.
Carl A. Palmer (286)........................850 Euclid Ave.
L. R. Reifsnider (638).........944 Union Commerce Bldg.
Max J. Rudolph (281)......................1105 Chester Ave.
Carlton Schultz (37)...............The B. F. Keith Bldg.
Elmer H. Seidman (705)..................14802 Madison Ave.
Alexander S. Taylor (142)....1930 Union Commerce Bldg.
V. C. Taylor. II (153)..........1930 Union Comerce Bldg.
William J. Van Aken (284)............1715 Euclid Ave.

Columbus

B. G. Ball (731)..............................580 E. Broad St.
Preston Cooke (551)..........................8 E. Broad St.
Charles F. Johnson (412)...................8 E. Long St.

Dayton

Sidney Eisenberger (704)...........286 Fourth St. Arcade
Rufus Lisle (438)........................704 Harries Bldg.

Geneva

J. Earl Miller (267)...........................Miller Bldg.

Massillon

Charles N. Hostetter (329)...........716 Lincoln Way, E.

Springfield

H. S. Kissell (5)................927 First Nat. Bk. Bldg.

Toledo

Claude A. Campbell (211)..............707 Ohio Bk. Bldg.
Edmund T. Collins (522)...............708 Jefferson Ave.
George P. Crosby (252)..................413 Madison Ave.
Howard Etchen (136)...........................725 Adams St.
Donald F. Hiett (396)....................622 Jefferson Ave.
John R. Schackne (529)....507 Produce Exchange Bldg.

OKLAHOMA

Tulsa

J. M. Allen (546)................................Beacon Bldg.
Clyde A. King (432).......................520 Beacon Bldg.

OREGON

Portland

Arthur C. Callan (674)......................320 Oregon Bldg.
Merle G. Campbell (675)...................511 Corbett Bldg.
Leroy D. Draper (676).................236 S. W. Broadway
H. A. Dryer (737)..............................603 Couch Bldg.
James R. Haight (677).............408 S. W. Fourth Ave.
F. C. McGowan (706)..........................603 Couch Bldg.
Henry Edward Reed (678)............805 Title & Tr. Bldg.
W. H. Ross (707)...........................413 S. W. Stark St.
Nat C. Soule (679)...........................1112 Porter Bldg.
A. G. Teepe (690)...................3114 N. E. Sandy Blvd.
Donald L. Woodward (680)............236 S. W. Broadway

PENNSYLVANIA

Bethlehem

William C. Bader (163).............214 Odd Fellows Bldg.

Erie

Carl G. Wright (361)..............204 Marine Bk. Bldg.

Harrisburg

Evan J. Miller (148).........................213 Locust St.

Lancaster

Harry W. Butts (114)......................24 E. Orange St.

Lansdowne

W. Raymond Evans (118).........19 N. Lansdowne Ave.

Lewistown

E. Dale Fisher (520)..........................136 Valley St.

Philadelphia

Philip N. Arnold (174)..................123 S. Broad St.
Boyd T. Barnard (237)..............Lincoln-Liberty Bldg.
Frederick A. Bond (380).............5433 Baltimore Ave.
E. L. Carlson (62).........The Parkway at Fairmont Ave.
C. Harris Colehower (145)..............5942 Chestnut St.
Frank P. Felton, Jr. (268).....914 Lincoln-Liberty Bldg.
Lionel Friedmann (565)....N.E. Cor. 15th & Locust Sts.
Joseph J. Greenberg (606)................Architects Bldg.
Samuel T. Hall (257).........................1500 Locust St.
Roy A. Heymann (362)......................213 S. Broad St.
C. Harry Johnson (238)........................Packard Bldg.
S. Craig Kane, Jr. (253)............502 Land Title Bldg.
John G. Keck (607)......................1622 N. Broad St.
Philip W. Kniskern (1)....................1604 Walnut St.
Albert H. Lieberman (726)....N.W. Cor. 15th & Locust Sts.
J. William Markeim (86)....................1424 Walnut St.
Frank H. Massey (549)......S. E. Cor. 13th & Green Sts.
Maurice R. Massey (276)....S. E. Cor. 13th & Green Sts.
J. Howard McLaughlin (372)...........5512 Florence Ave.
William I. Mirkil (226).....................1500 Walnut St.
Robert J. Nash (254).........................1214 Locust St.
Glyndon Priestman (420)..............18 W. Chelten Ave.
Richard J. Seltzer (255)..................15th & Locust Sts.
J. Willison Smith (239).....................100 S. Broad St.
Martin Stotz (55).......................514 Land Title Bldg.
James R. Taylor (728).......................4419 Walnut St.
Joseph W. Widing (648)....................100 S. Broad St.
Philip O. Widing (639)......................1604 Walnut St.
Ambrose J. Winder (207)....................1420 Walnut St.

Pittsburgh
Roy R. Cappe (608)....341 Fourth Ave.
H. Chidester (609)....618 Frick Bldg.
James W. Cotts (610)....307 Fourth Ave.
James W. Cree, Jr. (13)....211 Fourth Ave.
E. Herbert Gilg (552)....6605 Ridgeville St.
Fred J. Hettling (611)....820 Grant Bldg.
Albert O. Horner (720)....12 N. Diamond St.
Carl E. Koch (612)....20 Wabash Ave., West End
R. A. MacDowell (613)....345 Fourth Ave.
William Maisch (616)....307 Fourth Ave.
J. F. McClurg (614)....312 Fourth Ave.
R. L. McKallip (615)....411 Seventh Ave.
Thomas C. McMahon (640)....731 Grant Bldg.
L. W. Monteverde (641)....427 Fourth Ave.
Albert A. Murrer (584)....614 Plaza Bldg.
Donnell D. Reed (708)....504 City-County Bldg.
S. L. Seemann (657)....341 Fourth Ave.
Frank T. Trohaugh (617)....514 Oliver Bldg.

Scranton
C. G. Chappell (376)....Bliss Davis Bldg.

Wilkes-Barre
C. A. Leighton (135)....Deposit & Savings Bk. Bldg.
Edward L. Lewith (227)....428 Miners Bk. Bldg.
L. D. Scranton (100)....147 N. Franklin St.

Williamsport
Fred B. Wetzel (721)....25 W. Third St.
Louis A. Wetzel (709)....442 William St.

RHODE ISLAND

Pawtucket
Leo V. Boyle (722)....44 Broad St.

Providence
Hal Forrester Coombs (172)....211 Waterman St.
Richard A. Hurley (513)....723 Hospital Tr. Bldg.

TENNESSEE

Memphis
Elbert A. Cheek (547)....801-6 Columbian Mutual Tower
George W. Person (320)....
....Second Floor, Manhattan Bk. Bldg.
W. H. Prince (374)....1816 Poplar Ave.

Nashville
J. W. Denis (140)....535 Church St.
J. W. Graham (83)....930 Kirkwood Ave.

TEXAS

Amarillo
Robert Ricks (566)....Bivins Bldg.

Austin
Wilhelmine B. Sheffield (723)....207 W. Seventh St.

Beaumont
J. S. Edwards (444)....San Jacinto Bldg.

Dallas
Henry S. Miller (277)....405 Southland Life Bldg.
Lawrence Miller (386)....2729 South Blvd.
John W. Pat Murphy (384)....1420 Commerce St.

Fort Worth
Meredith R. Carb (354)....510 First Nat. Bk. Bldg.

Houston
W. G. Burchfield (274)....803 Second Nat. Bk. Bldg.
L. A. Casey (353)....508 Calhoun St.
A. R. Foster (619)....1525 Marshall St.
Brown C. Irwin (738)....703 Sterling Bldg.
Meredith H. James (681)....Esperson Bldg.

San Antonio
Paul W. Adams (355)....Builders Exchange Bldg.
A. H. Cadwallader, Jr. (352)..920 Nix Professional Bldg.
Charles W. Cart (724)....307 E. Pecan St.
C. Ray Davis (618)....716 Travis Bldg.
Claris M. Elmore (356)....200 Betty Jean St.
Harold W. Keller (620)....714 Travis Bldg.
Reginald W. Patton (317)....621 Travis Bldg.

UTAH

Salt Lake City
Werner Kiepe (567)....139 S. Second St., E.
Ralph B. Wright (739)....1117 Boston Bldg.

VIRGINIA

Newport News
Emanuel E. Falk (548)....117 26th St.

Richmond
John W. Bates (240)....723 E. Main St.
Henry S. Raab (260)....710 E. Main St.
J. Guthrie Smith (144)....329 Clovelly Rd.
Morton G. Thalhimer (221)....1013 E. Main St.

WASHINGTON

Bellingham
E. A. Wheeler (682)....1411 Commercial St.

Seattle
Charles P. Burnett (378)....14410 Third St., N. W.
Arthur E. Burr (576)....623 Second Ave.
Ralph H. Davis (577)....400 Skinner Bldg.
William A. Eastman (307)....414 University St.
R. C. Erskine (578)....2201 Northern Life Tower
Lloyd P. Hayworth (683)....200 17th Ave., N.
Ogden Johnson (658)....400 Skinner Bldg.
Walter G. McLean (346)....1108 Third Ave.
J. C. McQuigg (344)....1317 Boven Ave.
Vincent D. Miller (579)....337 Henry Bldg.
Ben J. Smith (343)....1222 Second Ave.
J. H. Sparkman (349)....1108 Third Ave.
Roy F. Taylor (659)....Seattle Tr. & Savings Bk.
Cecil S. Van Voris (369)....F.H.A., 1817 Exchange Bldg.
David T. Young (580)....511 Marion Bldg.

WEST VIRGINIA

Charleston
Charles Uhrig (79)....Box 1018

Wheeling
Harry C. Miller (725)....Rm. 2064, Board of Trade Bldg.

WISCONSIN

Madison
Stanley C. Hanks (642)....24 W. Mifflin St.
Paul E. Stark (643)....124 W. Mifflin St.

Milwaukee
Fritz W. Beck (581)....135 W. Wells St.
Lloyd M. Boyce (621)....735 N. Water St.
K. Lee Hyder (185)....525 E. Michigan St.
Robert F. Marty (622)....709 N. 11th St.
Arnold P. VanLoghem (691)....235 W. Galena St.

Racine
Victor E. Johnson (684)....433 Wisconsin St.
Kenneth E. Sarles (710)....218 Fifth St.

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The officers of the American Institute of Real Estate Appraisers announce with sincere regret the death of John J. Berry, M.A.I., Newark, N. J. Admitted July 1, 1932; died August 4, 1939.

JUNIOR MEMBERS

OCTOBER 1, 1939

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1. A Junior Member of the American Institute of Real Estate Appraisers holds membership in a Member Board of, or individual membership in, the National Association of Real Estate Boards.
2. Junior Members are not less than twenty-four years of age.
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